SENATE TAXATION
EXHIBIT NO. 3
1.14.09
Na

Montana Department of Revenue

Dan Bucks
Director

Brian Schweitzer
Governor

January 14, 2009

To: Senator Jeff Essmann
Senate Taxation Committee

From: Eugene Walborn, Administrator

Re: PPLM and Omimex Supreme and District Court Decisions

Per your request, please find the attached the PPL Montana and Omimex Canada Supreme and District court decisions.

The attached documents include:

PPL Montana LLC – Supreme Court Decision, December 2007
PPL Montana LLC – District Court Decision, April 2006
Omimex Canada, LTD – Supreme Court Decision, December 2008
Omimex Canada, LTD – District Court Decision, February 2007

DA 06-0477

IN THE SUPREME COURT OF THE STATE OF MONTANA

2007 MT 310

STATE OF MONTANA, DEPARTMENT OF REVENUE,

Petitioner, Appellee and Cross-Appellant

v.

PPL MONTANA, LLC,

Respondent and Appellant.

APPEAL FROM: District Court of the Eighth Judicial District,
In and For the County of Cascade, Cause No. BDV 2005-273
Honorable Dirk M. Sandefur, Presiding Judge

COUNSEL OF RECORD:

For Appellant:

Robert L. Sterup (argued), Holland & Hart, LLP, Billings, Montana

For Appellee and Cross-Appellant:

Brendan R. Beatty (argued), Special Assistant Attorney General, Charlena Toro, Special Assistant Attorney General, Montana Department of Revenue, Helena, Montana

C. A. Daw, Bosch, Daw and Ballard Chartered, Boise, Idaho

Argued and Submitted: June 13, 2007

Decided: December 4, 2007

Filed:

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Clerk

Justice Brian Morris delivered the Opinion of the Court.

¶1 PPL Montana, LLC (PPLM) appeals from the decision of the Eighth Judicial District Court, Cascade County, denying PPLM's claim that the Montana Department of Revenue (DOR) deprived PPLM of constitutional equal protection when it assessed PPLM's property taxes. DOR cross-appeals from the District Court's determination to uphold the State Tax Appeals Board's (STAB's) decision to lower DOR's appraisal of PPLM's property.

¶2 We review the following issues on appeal:

¶3 Did DOR's property tax assessment deprive PPLM of constitutional equal protection?

¶4 Did the District Court correctly affirm STAB's decision to lower DOR's appraisal of PPLM's property?

FACTUAL AND PROCEDURAL HISTORY

¶5 PPLM acquired most of the Montana Power Company's (MPC's) electric generation assets in 1999 as part of Montana's deregulation of its electric power industry. PPLM paid approximately $769,746,000 for 11 hydroelectric generation plants, a reservoir, the J.E. Corette Electric Generating plant, and partial interests in three coal-fired power plants, known as Colstrip units 1, 2, and 3.

¶6 DOR determined, pursuant to § 15-23-101(2), MCA, that PPLM was "operating a single and continuous property operated in more than one county . . . ." Accordingly, DOR "centrally assessed" PPLM's newly acquired property, rather than permitting the individual counties to assess that portion of PPLM's property within their jurisdictions.

¶7 DOR's administrative regulations require it to appraise the value of property owned by "centrally assessed companies," such as utilities, with the "unit method of valuation" "whenever appropriate." Admin. R. M. 42.22.111(1) (2007). DOR explains that it appraises utilities as a "unit" in light of the fact that the individual properties owned by utilities have no value, over and above their salvage value, except as integral parts of the very business in which they operate.

¶8 DOR applies the unit method of valuation to determine the utility's total value. DOR first considers the utility's tangible and intangible assets, regardless of where those assets may be located. Admin. R. M. 42.22.101(30)-(31) (2007). DOR then subtracts the utility's intangible personal property. Section 15-6-218, MCA; Admin. R. M. 42.22.110 (2007). DOR assigns a portion of the utility's total value to the utility's assets located in Montana based on the proportion of the utility's assets located in Montana as compared to the utility's total assets. Admin. R. M. 42.22.101(30)-(31) (2007). DOR considers that portion of the utility's value that it assigns to the utility's Montana-based assets to represent the "fair market value" of those assets for purposes of property taxes. *See* Admin. R. M. 42.22.121(1) (2007). DOR's appraisal must reflect "100% of [the property's] market value." Section 15-8-111, MCA.

¶9 DOR combines three valuation methods to appraise the utility's value as unit: the cost method, the income method, and the market method. Admin. R. M. 42.22.111(1) (2007). The cost method generally reflects what the utility paid for its assets or what it would have to pay to replace those assets. Admin. R. M. 42.22.112(1) (2007). The income method reflects the current value of the utility's historical or future income

streams. Admin. R. M. 42.22.114(1) (2007). The market method looks to the utility's stock value or the sale price for similar utilities in the past. Admin. R. M. 42.22.113 (2007). DOR uses its discretion to combine these various methods to arrive at a single value that best reflects the utility's fair market value. Admin. R. M. 42.22.111(1) (2007). DOR determines what weight to give to each method's result depending on such discretionary factors as whether the data that the particular method uses is sufficiently reliable. Admin. R. M. 42.22.111(2) (2007). DOR then, as described above, allocates to the utility's Montana-based assets that portion of the company's "unit value" that "represents the state's proper share of the market value of the centrally assessed company's operating property." Admin. R. M. 42.22.121(1) (2007).

¶10 DOR applied the unit method of valuation to PPLM's property to arrive at a total market value of PPLM's electric generation and pollution control equipment (PCE) for the years 2000, 2001, and 2002. Montana law classifies electric generation property and pollution control equipment separately as Class 13, § 15-6-156, MCA, and class 5, § 15-6-135, MCA, respectively, and declares different tax rates for these properties. DOR relied solely on the cost approach in the year 2000 to arrive at a market value of $706,736,726 for PPLM's electric generation property and $74,629,373 for PPLM's PCE, for a total fair market value of $781,366,099. DOR's data for its year 2000 assessment originated from PPLM's independently audited financial statements for 1999 and from PPLM's purchase price information for MPC's assets provided by PPLM's accountant, Delloite & Touche (D&T).

¶11 Another of PPLM's accountants, PricewaterhouseCoopers, later issued revised financial statements for the years 1999 and 2000. PPLM's revised financial statements included a different "book value" for its electric generation assets to reflect PPLM's "sale and lease-back" of its interest in Colstrip units 1, 2 and 3. PPLM had sold its interest in Coalstrip units 1, 2, and 3 to institutional investors and then immediately leased the properties back from those investors. PPLM analogized the sale and lease-back to a mortgage on a house, and argued that the arrangement had no effect on the actual market value of its assets for purposes of property taxes.

¶12 DOR determined that the sale and lease-back reflected a more accurate valuation of the Colstrip units, however, and, accordingly, raised its appraisal of PPLM's assets in 2001. DOR calculated a value of $769,234,685 for PPLM's electric generation property and a value of $69,240,822 for its PCE for a total fair market value of $838,475,507 in 2001.

¶13 DOR concluded in 2002 that it had sufficient income data from PPLM's operations to incorporate the income valuation approach into its assessment. DOR combined 10% of the income value approach with 90% of the cost approach to arrive at a value of $729,462,534 for PPLM's electric generating property, and a value of $93,401,040 for its PCE, for a total fair market value of $822,863,574.

¶14 PPLM challenged DOR's assessment of PPLM's electric generating property. PPLM and DOR attempted to negotiate a settlement over the next two years. The parties failed to reach a settlement, however, and PPLM appealed its tax assessments for the years 2000, 2001, and 2002 to STAB. PPLM challenged DOR's decision to assess

centrally its electric generation assets and DOR's ultimate valuation of those assets. PPLM also alleged that DOR had failed to exempt the proper amount of intangible personal property owned by PPLM, and that DOR had failed to classify the proper amount of its property as PCE. Lastly, PPLM alleged that DOR had deprived it of equal protection when it failed to equalize properly its property tax burden with other comparable electric generation facilities in Montana. PPLM pointed out that DOR had appraised other utilities—specifically Avista and Puget Sound Electric (PSE)—less on their comparable electric generation facilities.

¶15 STAB conducted hearings on April 26 through April 29, and June 3 through June 10, 2004 and issued its findings of fact and order on February 15, 2005. STAB concluded that DOR properly had determined that PPLM's electric generation facilities should be "centrally assessed." STAB disagreed with DOR's valuation, however, in light of the fact that DOR had relied on the sale and lease-back transaction as well as a short and anomalous income history.

¶16 STAB concluded that PPLM's taxable property value should be equal to $769,746,000 for all the years at issue as that was the fair market value that PPLM had reported to the Internal Revenue Service shortly after PPLM had purchased the property in 1999. STAB determined that DOR had calculated properly the intangible personal property exemption and the value of PPLM's class 5, PCE property. STAB then adjusted down the fair market value of PPLM's property for all three years. STAB declined to address the question of whether DOR had failed to equalize properly PPLM's property tax burden with that of similar utilities, however, in light of the fact that the question

involved property tax valuations of utilities not involved in the appeal and questions of constitutional law beyond its "normal purview."

¶17 DOR petitioned the District Court to review STAB's determination that PPLM's electric generation assets should be valued at $769,746,000, and to review STAB's subsequent adjustment of PPLM property's fair market value. PPLM petitioned the District Court to address the open question of whether DOR had assessed its property unequally in violation of the Equal Protection Clause of the Fourteenth Amendment of the United States Constitution and Article II, Section 4 of the Montana Constitution.

¶18 The District Court affirmed STAB's findings of fact and conclusions of law on all counts. The District Court also determined that DOR's assessment had not subjected PPLM to an unequal tax assessment in violation of its right to constitutional equal protection. DOR and PPLM appeal.

STANDARD OF REVIEW

¶19 We review a District Court's order affirming or reversing an administrative decision of STAB to determine whether the findings are clearly erroneous, and whether the agency correctly interpreted the law. *O'Neill v. Department of Revenue*, 2002 MT 130, ¶ 10, 310 Mont. 148, ¶ 10, 49 P.3d 43, ¶ 10. We review a district court's conclusions of law to determine whether those conclusions are correct. *Dukes v. Sirius Const., Inc.*, 2003 MT 152, ¶ 11, 316 Mont. 226, ¶ 11, 73 P.3d 781, ¶ 11.

DISCUSSION

¶20 *Did DOR's property tax assessment deprive PPLM of constitutional equal protection?*

¶21 PPLM argues that DOR has appraised its property at higher values than other similarly situated electric generation properties located in Montana. PPLM alleges, for example, that DOR has appraised PPLM's Thompson Falls dam at a slightly higher value than Avista's Noxon Rapids Dam, despite the fact that PPLM's Thompson Falls dam produces approximately one-seventh the electricity of Avista's Noxon Rapids Dam. PPLM also points out that DOR appraised its assets in tax year 2000 for almost $300 million more than the value that DOR had appraised those same assets at in 1999 when they were in the hands of MPC. PPLM alleges that DOR's inequitable treatment of its property compared to other similar properties deprives it of equal protection as guaranteed by the Equal Protection Clause of the United States Constitution and Article II, Section 4 of the Montana Constitution.

¶22 DOR explains that PPLM's relatively higher property tax burden derives from the fact that DOR did not appraise PPLM's property based on the fair market value of each individual piece of PPLM's property, such as an individual dam. DOR appraises PPLM's property using the "unit method of valuation." DOR uses the unit method of valuation method to determine the fair market value of PPLM as a "unit." DOR then proportionally allocates PPLM's total market value among its various assets. DOR explains that the relatively higher appraisal values of PPLM's properties as compared to Avista's and PSE's similar properties arise from the fact that these three companies have different total market values as a unit and, thus, their individual properties also will have different market values despite the fact that the individual properties may be similar physically.

¶23 DOR suggests that MPC's generation assets are considerably more valuable in the hands of PPLM because the Federal Energy Regulatory Commission has granted PPLM status as an exempt wholesale generator (EWG). An EWG is not subject to regulation by a state's public utility regulatory agency. An EWG may sell its electricity at whatever price the wholesale market will bear. And an EWG's profits are unrestricted by state regulation. Regulated utilities such as Avista, PSE, and the former MPC, on the other hand, have a limited opportunity to sell their electricity on the wholesale market and their profits are subject to state regulation. DOR asserts that PPLM's relatively higher unit value stems from the fact that MPC's electric generation facilities are worth more in PPLM's unregulated hands than those assets would be worth in a non-EWG's regulated hands. DOR points out that PPLM earned considerably higher profits than PSE and Avista for the tax years at issue.

¶24 We held in *Western Union Tel. Co. v. State Board of Equalization*, 91 Mont. 310, 7 P.2d 551 (1932), that the "unit method of valuation" passes scrutiny under the Equal Protection Clause of the United States Constitution. *Western Union*, 91 Mont. at 325, 7 P.2d at 554. Western Union owned and operated a worldwide network of telegraph lines, including a portion located in Montana. *Western Union*, 91 Mont. at 319, 7 P.2d at 551-52. Western Union argued that the State Board of Equalization (SBE) erroneously had determined its Montana property taxes. *Western Union*, 91 Mont. at 321, 7 P.2d at 552.

¶25 SBE had appraised the value of Western Union's Montana telegraph wires based on the total value of Western Union's worldwide telegraph system. *Western Union*, 91 Mont. at 320, 7 P.2d at 552. SBE first divided the total mileage of telegraph wire that

Western Union owned in Montana by the total mileage of telegraph wire that Western Union owned worldwide. SBE then multiplied this proportion by the total value of Western Union's worldwide system to determine the fair market value of Western Union's Montana assets. *Western Union*, 91 Mont. at 320, 7 P.2d at 552.

¶26 SBE had included "37,563 miles of submarine cables lying and being in the oceans of the world . . . ." in its calculation of the value of Western Union's worldwide system. *Western Union*, 91 Mont. at 320, 7 P.2d at 552. SBE's inclusion of the ocean cables raised the value of Western Union's worldwide system, and correspondingly, the value of its share of Montana cables in the worldwide system. Western Union challenged SBE's consideration of its ocean cables in the appraisal, in part, on equal protection grounds. *Western Union*, 91 Mont. at 320-21, 7 P.2d at 552.

¶27 This Court upheld the SBE's inclusion of the ocean cables noting that the SBE may consider "any value which that property has that is attributable to the fact that it is used in connection with and as part of an entire plant or system operated both within and without the state . . . ." *Western Union*, 91 Mont. at 323, 7 P.2d at 553. The Court explained that the "true and actual value of plaintiff's property is something more than an aggregation of the values of separate parts of it, operated separately, 'it is the aggregate of those values, plus that arising from a connected operation of the whole; and each part contributes, not merely the value arising from its independent operation, but its mileage proportion of that flowing from a continuous and connected operation of the whole." *Western Union*, 91 Mont at 324, 7 P.2d at 553 (quoting *Western Union Tel. Co. v. Taggart*, 163 U.S. 1, 16 S. Ct. 1054 (1896)).

¶28 The Court concluded with regard to the federal Equal Protection Clause that the plaintiff's constitutional claims were "wholly without merit . . . ." The Court explained that "[i]t is now settled by a long line of decisions that . . . the equal protection clause is not violated by prescribing a different rule of taxation for [railroads, utilities, etc.] than for concerns engaged in other lines of business." *Western Union*, 91 Mont at 325, 7 P.2d at 554. The Court concluded that the federal Equal Protection Clause does not prevent a State from assessing taxes on a company's property based on the use to which a company puts those assets in its larger system or business.

¶29 We can see no reason—and PPLM suggests none—as to why an analysis pursuant to Article II, Section 4 of the Montana Constitution would require a different result. We have drawn no distinction between the protections offered by Article II, Section 4 of the Montana Constitution and those offered by the Equal Protection Clause of the United States Constitution when analyzing alleged discrimination between similarly situated taxpayers. *Roosevelt v. Montana Dept. of Revenue*, 1999 MT 30, ¶¶ 16-46, 293 Mont. 240, ¶¶ 16-46, 975 P.2d 295, ¶¶ 16-46; *Kottel v. State*, 2002 MT 278, ¶ 47, 312 Mont. 387, ¶ 47, 60 P.3d 403, ¶ 47; *Montana Dept. of Revenue v. Barron*, 245 Mont. 100, 111, 799 P.2d 533, 540 (1990); *see also* 71 Am. Jur. 2d § 340 (2007) (explaining that there is nothing in the unit method of valuation that is inherently opposed to either the federal or the various state constitutions); *Beaver County v. Wiltel, Inc.*, 995 P.2d 602, ¶¶ 24-26 (Utah 2000) (holding that central assessment by the unit method of valuation did not violate the Equal Protection Clause of the United States Constitution or the "uniform operation of laws provision" in the Utah constitution).

¶30 Most of PPLM's arguments amount to an invitation for this Court to reconsider the long-settled constitutionality of the unit method of valuation. PPLM argues, for example, that DOR has applied the unit method of valuation to assess the electric generation assets of PPLM, PSE, and Avista based on the value that those assets have in the hands of the individual utilities rather than the value that those assets would have as individual properties on the open market. PPLM points to the fact that its assets were valued at $300 million less in the hands of MPC. PPLM also contends that its tax burden on its electric generation property has increased by 82% over the years from 1999-2002, while the tax burden on PSE's and Avista's electric generation property has declined. PPLM concludes that DOR's unit method of valuation amounts to a prima facie deprivation of equal protection.

¶31 We already have approved of the fact, however, that the unit method of valuation inherently values a property based on its value in the hands of its current owner. *Western Union*, 91 Mont. at 324, 7 P.2d at 553. Our precedents recognize that the fair market value of a piece of property, that is an integral part of a larger system, derives from its value as a part of the larger system. *Western Union*, 91 Mont. at 324, 7 P.2d at 553. We recognize that for such systems the "value-in-use" of the particular piece of property equates to the fair market value of that property for property tax purposes. *Western Union*, 91 Mont. at 324, 7 P.2d at 553. We find nothing constitutionally significant in the bare fact that DOR appraises the fair market value of the same electric generation assets differently when those assets are owned by different utilities.

¶32 PPLM also argues, however, that DOR has applied the otherwise constitutional unit method of valuation in a discriminatory manner. PPLM asserts that DOR created an irrational classification between utilities that qualify as EWGs and the more traditional regulated utilities. PPLM also asserts that DOR applied the unit method of valuation in a manner that amounts to an impermissible "welcome stranger" assessment as held unconstitutional in *Allegheny Pittsburgh Coal Co. v. County Comm'n*, 488 U.S. 336, 109 S. Ct. 633 (1989). We address each argument in turn.

¶33 The basic rule of equal protection "is that persons similarly situated with respect to a legitimate governmental purpose of the law must receive like treatment." *Rausch v. State Compensation Ins. Fund,* 2005 MT 140, ¶ 18, 327 Mont. 272, ¶ 18, 114 P.3d 192, ¶ 18. We have held that "the first prerequisite to a meritorious claim under the equal protection clause is a showing that the state has adopted a classification that affects two or more similarly situated groups in an unequal manner." *Powell v. State Compensation Ins. Fund,* 2000 MT 321, ¶ 22, 302 Mont. 518, ¶ 22, 15 P.3d 877, ¶ 22.

¶34 PPLM alleges that Avista, PSE, and PPLM all are similarly situated with respect to the purpose of the law at issue. The unit method of valuation as described in DOR's administrative regulations constitutes the law at issue. Admin. R. M. 42.22.101(30) (2007), explains that the unit method of valuation "is a method for determining the market value of a centrally assessed company." Section 15-23-101, MCA, defines centrally assessed company as "a corporation or other person operating a single and continuous property operated in more than one county or more than one state . . . ." DOR's regulations explain that the unit method of valuation "involves appraising, as a

going concern and as a single entity, the entire unit, wherever located, then deducting the intangible personal property value and then ascertaining the part thereof in this state." Admin R. M. 42.22.101(30) (2007). This regulation serves to determine the market value of a company that owns property operated as a single system throughout more than one county or state. Section 15-23-101, MCA. We agree that Avista, PSE, and PPLM all are similarly situated with respect to this law in that they all operate electric generation properties as a system over more than one county or state.

¶35 We cannot conclude under these circumstances, however, that DOR has treated PPLM, Avista, and PSE in an unequal manner. PPLM admits that DOR "did not consider, evaluate, or otherwise take into account, in any fashion, . . . [the extent to which PPLM, Avista, or PSE participated in wholesale markets] when assessing PPLM's properties in 2000-2002." PPLM's admission makes sense in light of the fact that DOR appraised the value of PPLM primarily on the value that PPLM paid for its generation assets and, to some extent, the income that PPLM generated from those assets. Whether PPLM, Avista, or PSE participated in wholesale markets played no direct role in DOR's appraisal of these utilities. STAB concluded, in fact, that "DOR utilized the same methodology and approach in appraising the Montana taxable properties owned by PPLM, Puget, and Avista." PPLM does not challenge this finding on appeal.

¶36 DOR—along with the District Court—suggests that PPLM's higher unit value probably derives from the fact that PPLM operates as an EWG and, thus, operates in a comparatively more profitable regulatory environment. DOR's speculation as to the reason for PPLM's higher value as a going concern, however, does not amount to unequal

treatment of Class 13 utilities. DOR has treated all the utilities at issue similarly by calculating their value based on its analysis of the cost, market and income indicators, regardless of whether the utilities' status as an EWG or a non-EWG raises or lowers the value of those indicators. The record fails to support PPLM's allegation that DOR has singled out PPLM for unequal treatment.

¶37 PPLM nevertheless insists that the "undeniable" effect of DOR's application of the unit method of valuation in this case amounts to the "welcome stranger" method found constitutionally impermissible in *Allegheny*. The county tax assessor in *Allegheny* taxed property within the county based solely on the value for which the most recent owner had purchased the property, regardless of the property's present market value. *Allegheny*, 488 U.S. at 338, 109 S. Ct. at 635. The assessor's method "systematically produced dramatic differences in valuation between petitioners' recently transferred property and otherwise comparable surrounding land." *Allegheny*, 488 U.S. at 341, 109 S. Ct. at 637. The Court found that this treatment violated constitutional equal protection, noting that the petitioner's property "has been assessed at roughly 8 to 35 times more than comparable neighboring property." *Allegheny*, 488 U.S. at 344-46, 109 S. Ct. at 638-39.

¶38 PPLM asserts that DOR—as well as STAB—likewise based its unit valuation of PPLM entirely on the price at which PPLM purchased MPC's generation assets. PPLM explains that DOR valued the electric generation assets under MPC at their historic cost minus depreciation, while DOR valued the same assets pursuant to PPLM's more recent purchase. PPLM also alleges that DOR valued Avista's and PSE's properties using their historical cost minus depreciation. PPLM contends that DOR's decision resulted in a

valuation of its electric generation assets at almost $800 million. By contrast, DOR valued those same assets at only around $500 million in the previous year, under the ownership of MPC. PPLM alleges that DOR's focus on the cost factor when it applied the unit method of valuation amounts to the "welcome stranger" method found unconstitutional in *Allegheny*.

¶39 DOR's method bears little resemblance to the method used in *Allegheny*. DOR did not appraise PPLM solely based on its purchase price. DOR considered the price that PPLM paid for its assets, the income that PPLM earned from its assets, and what similar assets might sell for on the open market. Admin. R. M. 42.22.111(1) (2007). DOR relied on PPLM's purchase price only after DOR had determined that PPLM's purchase price represented the most accurate indicator of the current market value of PPLM's assets. DOR's method requires it to use the most accurate indicators as they become available. Admin. R. M. 42.22.111(1) (2007). DOR, for example, in part, relied on PPLM's income for its 2002 appraisal. The County assessor in *Allegheny*, to the contrary, relied solely on the purchase price of the property at issue and completely disregarded any other indicators of market value. *Allegheny*, 488 U.S. at 340, 109 S. Ct. at 636.

¶40 PPLM has failed to demonstrate that DOR's initial reliance on purchase price will result in the type of systematic undervaluation of property that the Court determined unconstitutional in *Allegheny*. PPLM points only to the absolute difference in the assessed value of its property as compared to the assessed value of Avista's and PSE's property. We already stated above, however, that similar pieces of property likely will be valued differently under the unit method of valuation in light of the fact that DOR values

an individual property based on the total market value of the system in which that property operates. We would expect that PPLM's electric generation dam would be valued differently than a comparable dam owned by Avista or PSE as both the utilities likely are to have a different total market value, especially in light of the fact that PPLM operates as EWG, while PSE and Avista operate as regulated utilities.

¶41 We conclude that the District Court correctly determined that PPLM has failed to establish that DOR's use of the unit method of valuation deprives PPLM of constitutional equal protection. *Dukes*, ¶ 11. PPLM mistakenly focuses on the fact that DOR appraised its properties at different values than other centrally assessed utilities. Its argument founders on the fact that DOR does not tax properties owned by utilities based on the sum of their properties' respective market values, independent of the system in which the properties operate. DOR taxes Montana properties owned by utilities based on the value of the system in which those properties operate. Admin. R. M. 42.22.101(30) (2007). Courts long have considered the constitutional validity of the unit method of valuation as settled law. *Western Union*, 91 Mont at 325, 7 P.2d at 554. We decline PPLM's invitation to revisit the constitutionality of the unit method of valuation here. PPLM also has failed to show that DOR has applied the unit method of valuation in a manner that discriminates against its status as an EWG or in a manner that intentionally and systematically undervalues similarly situated properties.

¶42 *Did the District Court correctly affirm STAB's decision to lower DOR's appraisal of PPLM's property?*

¶43 DOR alleges first that the District Court erred in affirming STAB's decision to ignore PPLM's sale and lease-back transaction in its valuation of PPLM's electric generation assets. DOR asserts that the sale and lease-back transaction constituted an integral part of PPLM's purchase of MPC's electric generation assets. DOR argues that STAB substantially undervalued PPLM's assets when it failed to consider the sale and lease-back's effect on the value of PPLM's property.

¶44 STAB found that the sale and lease-back served "to secure necessary financing for PPLM." STAB determined that "the sale lease-back was nothing more than a financing mechanism and added no additional value to the property." STAB concluded that "there is insufficient support to suggest this transaction increased the value of the property."

¶45 We defer to STAB's findings unless they are clearly erroneous. *O'Neill,* ¶ 10. We previously have stated that "[t]ax appeal boards are particularly suited for settling disputes over the appropriate valuation of a given piece of property, and the judiciary cannot properly interfere with that function." It is not our function "to act as an authority on taxation matters." *Dept. of Revenue v. Grouse Mt. Development*, 218 Mont. 353, 355, 707 P.2d 1113, 1115 (1985).

¶46 DOR argues that STAB erred in failing to recognize that the sale and lease-back transaction represents a single transaction for taxation purposes. DOR fails to explain, however, why treating the sale and lease-back as part of the purchase instead of a separate transaction undermines STAB's finding that the sale and lease-back constituted a financing scheme that had no effect on the fair market value of the property. We cannot

conclude under these circumstances that STAB's finding is clearly erroneous. *O'Neill,* ¶ 10.

¶47 DOR argues, in the alternative, that STAB failed to account for $40 million in investments that PPLM made to its electric generation assets between 2000 and 2001. DOR asserts that STAB accidentally removed these investments when it excised the value of the sale and lease-back transaction from DOR's appraisal. DOR explains that without these investments STAB has underestimated the fair market value of PPLM's assets for the years 2001 and 2002.

¶48 PPLM counters that DOR failed to raise this argument in the District Court. DOR alleged in the District Court that STAB had ignored several "material changes" in PPLM's assets that occurred in 2001 and 2002, including significant income earned by the property, investment, depreciation, and amortization of liabilities PPLM assumed in its purchase of the assets. DOR made no attempt, however, to direct the District Court to the magnitude of these "material changes" or explain in any detail what effect they might have on PPLM's fair market value for the 2001 and 2002 tax years. DOR stipulated to STAB's finding that the parties did not establish at trial the liabilities that PPLM assumed in its purchase of MPC's electric generation assets.

¶49 DOR now asks this Court to review STAB's alleged failure to account for PPLM's $40 million in investments. DOR directs this Court's attention to various minutiae in STAB's accounting calculations and explains their significance in detail. We decline to second guess the District Court on tax accounting details, however, that it never had a fair chance to consider. *Ford v. State*, 2005 MT 151, ¶ 12, 327 Mont. 378, ¶ 12, 114 P.3d

244, ¶ 12. Moreover, we agree with the District Court that DOR essentially waived this argument when it stipulated that a portion of these "material changes" were not established at trial.

¶50 Affirmed.

/S/ BRIAN MORRIS

We concur:

/S/ JAMES C. NELSON
/S/ PATRICIA COTTER
/S/ W. WILLIAM LEAPHART
/S/ BRAD NEWMAN
District Court Judge Brad Newman
sitting for Chief Justice Karla M. Gray

Justice John Warner concurs.

¶51 I concur in the result of the Court's opinion, but not with all that is stated therein. PPLM complains that it is a violation of equal protection for DOR to appraise its property as worth more than the comparable properties owned by PSE and Avista. PPLM is correct that the electrical generating plants owned by PSE and Avista are not assessed at the value they would bring on the open market in a sale between a presumed willing buyer and a presumed willing seller. The fair market value of a specific piece of property will not be less than a willing buyer will pay for it on the open market. If the owner of the property is willing to sell it, such owner might demand more for the property than a willing buyer offers, but surely the owner will not demand less than the offer. The price that PPLM recently paid for one-half of

the Colstrip units in question is indeed powerful evidence of the value of PSE's one-half interest in the same generating plants.

¶52 However, Montana tax law provides that in the present instance the properties of PPLM, PSE and Avista are not necessarily "comparable property." Thus, the law provides that these properties need not be assessed equally. Section 15-7-112, MCA, says:

> The same method of appraisal and assessment shall be used in each county of the state to the end that *comparable property with similar true market values* and subject to taxation in Montana shall have substantially equal taxable values at the end of each cyclical revaluation program hereinbefore provided. [Emphasis added.]

¶53 Section 15-1-101(1)(e), MCA, states:

> The term "comparable property" means property that:
> (i) has similar use, function, and utility;
> (ii) is influenced by the same set of *economic trends* and physical, *governmental*, and social *factors*; and
> (iii) has the potential of a similar highest and best use. [Emphasis added.]

¶54 As the District Court aptly concluded, because PPLM operates in an unregulated market, whereas PSE and Avista operate in regulated markets, their properties are not necessarily "comparable" under Montana law because they are not "influenced by the same set of economic trends and . . . governmental . . . factors[.]" The District Court explained in detail:

> However, under the regulatory status quo, the electric generation properties of PPLM and PSE/Avista are <u>not</u> currently subject to, and influenced by, the same set of regulatory and economic restrictions, factors, and environment. PPLM and PSE/Avista operate in substantially different regulatory and economic environments. As an EWG, PPLM may sell an unlimited amount of power on the wholesale market for profit at market rates. In the regulated environment in which they operate, PSE and Avista may not profit above the reasonable rate of return that state regulatory agencies authorize them to recover on their investments. Consequently, PPLM's Montana electric

generation assets have been substantially more profitable and have substantially more profit-potential than those of PSE/Avista under the regulatory status quo.

¶55 While PPLM complains the District Court erred in determining that their property was not comparable with that of PSE and Avista, the District Court's conclusion was based on the law.

¶56 The basic rule of equal protection is that "persons similarly situated with respect to a legitimate governmental purpose of the law must receive like treatment." *Rausch v. State Compen. Ins. Fund*, 2005 MT 140, ¶ 18, 327 Mont. 272, ¶ 18, 114 P.3d 192, ¶ 18. By enacting the above referenced statutes, which define what may be considered "comparable property," the legislature has, in effect, provided that property owned by a regulated utility may be appraised at a lesser value for tax purposes than that same property owned by an unregulated utility. Thus, the legislature has determined that PPLM, PSE and Avista are not similarly situated and there is no equal protection violation. Like many things in the law of taxation, the disparate valuation of the properties in question may not be entirely logical. But, as noted by the District Court, there is a rational basis for the different valuations and they are not illegal.

¶57 While assigning a greater value to PPLM's properties than to PSE's or Avista's property creates a fictional result, DOR's valuation is not a violation of equal protection. Therefore, I must concur in the result of the Court's decision.

/S/ JOHN WARNER

Justice Jim Rice concurring.

¶58 I agree with the conclusion reached in Justice Warner's concurrence that the statutes permit the distinctions which were drawn by the DOR between the utility properties at issue here. I would only note that the Legislature did not *mandate* that such particular distinctions be made, but, rather, *authorized* them to be made pursuant to the very broad discretion regarding the assessment of this tax which it delegated to DOR. The breadth of this discretion is quite notable.

¶59 The citizenry may assume that the Legislature sets tax levels for major corporations, but, as this case illustrates, that may be true only in a broadly general sense. Under the DOR's "unit method of valuation," including the application of such factors as trending indices, depreciation and use analyses, the DOR unilaterally increased PPL's property value assessment by a phenomenal 50 percent in one year—with corresponding increases in PPL's tax bill. I say that the DOR acted "unilaterally" because this large tax increase was accomplished without the passage of any legislation by the Legislature for the purpose of increasing taxes in this manner. Indeed, not a single legislative vote was cast. Significant impacts such as this may explain why the bureaucracy has been referred to by some as "the fourth branch of government." As with any broad delegation of authority, there is a potential for abuse.

¶60 DOR defends its currently employed version of the unit method of valuation and argues it is constitutional. I do not necessarily disagree, but in my view that is not the real issue here. The issue is whether the DOR, in applying the factors *within* the unit method, has exercised its discretion in a way that offends equal protection. However, PPL's challenge,

which focuses on the outcome—that is, the disparities in the respective tax bills of the utilities involved—simply has not proved a violation of equal protection premised upon a misapplication of the unit method's factors. PPL does not contest STAB's finding that DOR used an equal approach in applying the unit method to assess the properties owned by PPLM, Puget and Avista. Given that there is no dispute over this factual finding, I concur in the Court's decision to affirm. Whether a challenge focused upon DOR's application of individual factors within the unit method of valuation would establish a constitutional violation is a question which may be raised another day.

/S/ JIM RICE

MONTANA EIGHTH JUDICIAL DISTRICT COURT, CASCADE COUNTY

MONTANA DEPARTMENT OF REVENUE, a Department of the State of Montana, Petitioner, -vs- PPL MONTANA, LLC, Respondent.	Cause No.: BDV-05-273(d) **ORDER UPON JUDICIAL REVIEW OF STATE TAX APPEAL BOARD DETERMINATION IN RE TAX YEARS 2000-02**

Pursuant to §§ 15-2-303 and 2-4-702, MCA, the Montana Department Revenue (Department) petitioned for judicial review of the determination of the State Tax Appeal Board (STAB) for tax years 2000-02 in the matter of PPL Montana v. MDOR, Docket Nos. SPT-2002-4 and SPT 2002-6.[1] Upon completion of briefing, the above-captioned matter came on for hearing on March 21, 2006. Upon due consideration of the factual record, briefs, and oral argument, the Court hereby affirms STAB's adjustments to the Department's 2000-02 assessments of Class 13 and Class 5 property owned or operated by *PPL Montana, LLC* (PPLM). The Court further concludes that, as applied to PPLM for tax years 2000-02 and as

[1] The STAB decision, in the form of its *nunc pro tunc* findings of fact, conclusions of law, and order, dated February 15, 2005, is filed as an exhibit to Doc. 1 in this matter.

adjusted by STAB, the Department's appraisal methodology and resulting assessments for 2000-02 did not unequally assess PPLM's Montana property in relation to other electric generation properties in Montana and did not result in a disparate tax burden in violation of the equal protection clauses of the Fourteenth Amendment of the U.S. Constitution and Mont. Const. art. II, § 4.

FACTUAL AND PROCEDURAL BACKGROUND

In order to resolve the disputed property tax issues in this case it is first necessary to understand the legal and economic framework from which they arise. Pursuant to Part II of the Federal Power Act, 16 U.S.C. §§ 824-824m, the Federal Energy Regulatory Commission (FERC) has exclusive plenary authority to regulate the generation, transmission, and sale at wholesale of electric energy in interstate commerce, except as Congress has explicitly made subject to regulation by the States. See 16 U.S.C. § 824; Public Utility Dist. No. 1 of Grays Harbor v. IdaCorp, Inc. (9th Cir. 2004), 379 F.3d 641, 646; Transmission Agency of No. Calif. v. Sierra Pac. Power Co. (9th Cir. 2002), 295 F.3d 918, 928-930. In 1992, Congress enacted Title VII of the Energy Policy Act of 1992 empowering FERC to provide for deregulation of the electric-power industry and move it "toward a fully competitive market system" by promoting "greater competition in bulk power markets" through encouragement of "new generation entrants, known

as exempt wholesale generators (EWGs)," and providing open access to the electrical transmission system. 61 Fed.Reg. 21,546 (May 10, 1996) (FERC Order No. 888). Accordingly, in 1993, FERC established rules for electrical generators to obtain FERC-approved EWG status, as defined by 15 U.S.C. § 79z-5a. See 58 Fed.Reg. 8897 (Feb. 18, 1993) (FERC Order No. 550); see also 61 Fed.Reg. 21,547 (May 10, 1996) (FERC Order No. 888).

By 1996, FERC determined that additional reform was necessary to balance the competing interests of continuing deregulation to establish a more open and competitive market for new, non-traditional generators while at the same time ensuring the continued reliability of the national power supply system and not competitively disadvantaging traditional electric generators. See 61 Fed.Reg. 21,550 (May 10, 1996) (FERC Order No. 888). Accordingly, in 1996, FERC issued Order No. 888 which:

> functionally combined FERC regulation of rates with FERC regulation of transmission capacity . . . by [regulating] rates not by setting them directly, but rather by setting rules requiring open access to transmission lines at uniform, openly disclosed, rates. [Citation omitted]. These open policies as to transmission capacity, FERC expects, will result in rates set at a competitive level. [Citation omitted]. Thus, FERC's regulation of interstate rates now operates through FERC's regulation of open access to transmission capacity.

Transmission Agency of No. Calif., 295 F.3d at 931. *Inter alia*, FERC Order No. 888 required "functional unbundling of wholesale generation and transmission services" to "implement non-

discriminatory open access transmission." 61 Fed.Reg. 21,551 (May 10, 1996) (FERC Order No. 888). Accordingly, FERC recognized that this "functional unbundling" requirement "would accommodate, but not require, corporate unbundling (which could include selling generation or transmission assets to a non-affiliate (divestiture) or the less aggressive step of establishing separate corporate affiliates to manage a utility's transmission and generation assets)." Id. at 21,551-52. Consequently, in order to be eligible to operate as an unregulated EWG and charge market-based rates on the wholesale market, an electrical generator must apply and obtain approval from FERC in accordance with federal law. Grays Harbor, 379 F.3d at 649. Thus, as pertinent here, the net effect of federal deregulation was that it provided for the functional and corporate unbundling of wholesale electric generation and transmission services and for FERC-authorized EWGs to sell electricity at wholesale prices on the open market.

In response, the 1997 Montana Legislature enacted legislation deregulating the electric-power industry in Montana in accordance with federal deregulation. See Title 69, Chapter 8, MCA (Montana Electric Industry Restructuring & Customer Choice Act). The Montana Act provided for "utilities such as" the Montana Power Company (MPC) "to separate the generation, distribution, and transmission functions of their operations" and for deregulation of their generation function while preserving the Montana Public

Service Commission's regulatory authority over distribution and transmission functions. Montana Power Co. v. Montana Public Service Comm., 2001 MT 102, ¶ 5, 305 Mont. 260, ¶ 5, 26 P.3d 91, ¶ 5. The Montana Act charged the Montana Public Service Commission:

> with administering this process of restructuring and deregulation. Thus, the Act requires utilities to file a deregulation "transition" plan with the Commission that comports with various deregulation requirements under the Act. In turn the Commission must review and approve of the plan pursuant to the mandates under the Act, including issuing a final order approving, modifying, or denying the transition plan.

Id. at ¶¶ 6, 46, and 49. As recognized by the Montana Supreme Court, the underlying Darwinian principle of deregulation is that "infusion of competition will naturally select and reward the strongest and fittest utilities for the ultimate benefit of the consumer." Montana Power Co., ¶ 45.

In March of 1998, in accordance with federal and state deregulation, MPC initiated a competitive bidding process to divest its electric generation assets. (Ex. TT, p. 57-58). In the course of this process, MPC solicited 263 potential bidders, focused on a subset of 47 qualified bidders, and ultimately selected PPLM's parent corporation as the successful bidder. (Id.). On or about December 17, 1999, pursuant to the terms of a negotiated purchase agreement with MPC, PPLM acquired and commenced operation of most of MPC's electric generation

facilities, including 11 hydroelectric generation plants, a reservoir, the J.E. Corette Electric Generating Plant, and partial interests in three coal-fired power plants known as Colstrip Units 1, 2, and 3. (STAB FF 6 and 13).

For tax years 2000-02, the Department assessed PPLM as a centrally assessed electric facility pursuant to Title 15, Chapter 23, Part 3, MCA. (STAB FF 26). Under Case No. SPT-2002-4, PPLM appealed its 2000-01 property tax assessments to STAB. (STAB FF 3). PPLM subsequently appealed its 2002 assessment under Case No. SPT-2002-6. (STAB FF 3). For hearing and decision, STAB consolidated PPLM's appeals for 2000-02. (STAB FF 5). Upon consolidation, STAB considered the following issues on appeal:

(1) whether PPLM's property was properly subject to central assessment under § 15-23-101(2), MCA;

(2) whether the Department properly valued PPLM's electric generation property (Class 13 property) for tax years 2000-02;

(3) whether the Department properly valued PPLM's pollution control equipment (Class 5 property) for tax years 2000-02;

(4) whether the Department exempted the proper amount of PPLM's property from taxation for tax years 2000-02; and

(5) whether the Department properly equalized the value of PPLM's interest in Colstrip Units 1 and 2 with its co-owner, *Puget Sound Energy*, for tax years 2000-01, and whether the Department properly equalized PPLM's hydroelectric facilities with those owned by *Avista Corporation* for tax year 2002.

(STAB FF 2-4).

As a threshold matter, STAB ruled that PPLM's property was properly subject to central assessment under § 15-23-101(2), MCA. (STAB Order, p. 27-30, 39-40, and 42). Neither party appeals this determination upon district court review. As to valuation, STAB found that the Department used a unit assessment methodology to determine a system valuation of a company's assets as an entire business unit through consideration and correlation of various value indicators under the cost approach, income approach, and market approach. (STAB FF 39-40; Day 6 Tr., p. 109-19; STAB Order, p. 30-31).[2] Upon consideration of various valuations under each of these approaches, STAB determined that the total value for all classes of PPLM property for 2000-02 was the value PPLM reported to the Internal Revenue Service (IRS) as the "aggregate fair market value" of the acquired assets ($769,746,00). (STAB Order, p. 30-35). The Department disputes this determination on review.

Based on PPLM's failure to include any value for business goodwill in its financial statements and post-acquisition filings with the IRS and Securities and Exchange Commission (SEC), STAB ruled that the Department properly concluded that PPLM was not entitled to any additional exemption for business goodwill in excess of the 10% default value under § 15-6-218, MCA, and

[2] See also §§ 42.22.101(30), 42.22.101(31), 42.22.101(7), 42.22.111, 42.22.1309, 42.22.1315, 42.22.112, 42.22.113, and 42.22.114 ARM.

§ 42.22.110, ARM. (STAB Order, p. 35-36 and 41). Neither party appeals this determination on review.

STAB further found that the Department's 2000-02 assessments properly "stepped-up" the value of PPLM's pollution control equipment (PCE) from the value assessed to MPC at the time of acquisition by PPLM. (STAB Order, p. 37). Based on the approximate 10% ratio of the Department's 2000-02 PCE assessments to the total values apportioned to the counties for 2000-02, STAB determined that the proper PCE value should be 10% of the total value apportioned to the counties. (STAB Order, p. 36-37). The Department disputes this determination on review.

Based on its determination that the total value for all classes of PPLM property for 2000-02 was $769,746,000, STAB concluded that the Department failed to assess PPLM's property at 100% of fair market value as required by § 15-8-111(1), MCA. (STAB Order, p. 40). Thus, based on its determination that the total value of PPLM's property for 2000-02 was $769,746,000 and that the total value of the pollution control equipment was 10% of the total system value, STAB adjusted the Department's 2000-02 assessments as follows:

FMV - STAB DETERMINATION (FMV Assessed To Counties)			
Year	Class 13(EGP)	Class 5(PCE)	Total FMV
2000	$685,972,665	$76,219,185	$762,191,850
2001	$649,874,213	$72,208,246	$722,082,459
2002	$625,566,526	$69,507,392	$695,073,918

(STAB Order, p. 35, 37, and 42). On review, the Department asserts that STAB's total system valuations and PCE valuations are erroneous.

Although STAB speculated on PPLM's assertion that the Department unequally assessed PPLM's interest in Colstrip Units 1 and 2 in 2000-01 and its hydroelectric facilities in 2002 in relation to similar properties owned by *Puget Sound Energy* (PSE) and *Avista Corporation* (Avista), STAB held that it had no jurisdiction to address constitutional issues or to address valuations of other taxpayers not before it. (STAB Order, p. 37-39). Consequently, on review, PPLM again asserts that Montana has unequally assessed its property in violation of the equal protection clauses of the Fourteenth Amendment of the U.S. Constitution and Mont. Const. art. II, § 4.

ANALYSIS

The parties present the following issues in this case:

(1) Did STAB have jurisdiction to adjust the Department's appraised value of PPLM's property for tax years 2000-01 ?

(2) Did STAB err in adjusting the Department's 2000-01 valuations of PPLM property ?

(3) Did STAB abuse its discretion in adjusting the Department's valuations of PPLM's pollution control equipment for tax years 2000-02 ?

(4) Did Montana unequally assess PPLM in relation to the same or similar electric generation property owned by PSE and Avista thereby resulting in an disparate tax burden in violation of the equal protection clauses of the Fourteenth Amendment of the U.S. Constitution and Mont. Const. art. II, § 4 ?

The first three issues arise under § 15-2-303, MCA, (judicial review of STAB decisions). The fourth issue arises as a matter of original district court jurisdiction.

I - STANDARD OF REVIEW OF STAB DECISION

Upon judicial review, the district court may affirm, reverse, remand, or modify a STAB determination in accordance with the provisions of § 15-2-303, MCA, and Title 2, Chapter 4, Part 7, MCA (Montana Administrative Procedure Act). §§ 15-2-301(5) and 2-4-704(2), MCA. The court may reverse or modify a STAB decision if the substantial rights of a party have been prejudiced because the STAB findings of fact or conclusions of law are:

(1) in violation of constitutional or statutory law;

(2) in excess of STAB's statutory authority;

(3) based upon a procedural or substantive error of law;

(4) clearly erroneous in view of the reliable, probative, and substantial evidence on the whole record; or

(5) arbitrary or capricious or characterized by abuse or clearly unwarranted exercise of discretion.

§ 2-4-704(2)(a), MCA. The court may also reverse or modify a STAB decision if the substantial rights of a party have been prejudiced because STAB failed, upon the request of a party, to make findings of fact upon an issue essential to the decision. § 2-4-704(2)(b), MCA.

The scope of district court review is limited to review of the underlying record except that the court may take additional proof of alleged procedural irregularities and may, upon a showing of good cause, take supplemental evidence. §§ 2-4-704(1) and 15-2-303(5), MCA. The standard of review for STAB's conclusions of law is whether the conclusions are correct. Ostergren v. MDOR, 2005 MT, 30, ¶¶ 11 and 15, 319 Mont. 405, ¶¶ 11 and 15, 85 P.3d 738, ¶¶ 11 and 15; O'Neill v. MDOR, 2002 MT 130, ¶ 10, 310 Mont. 148, ¶ 10, 49 P.3d 43, ¶ 10; Farmers Union Central Exch., Inc. v. MDOR (1995), 272 Mont. 471, 474, 901 P.2d 561, 563; Leahy v. MDOR (1994), 266 Mont. 94, 97, 879 P.2d 653, 655. In contrast, the standard of review for STAB's findings of fact is whether they are clearly erroneous. Ostergren, ¶¶ 11 and 15; O'Neill, ¶ 10; Leahy, 266 Mont. at 97, 879 P.2d at 655. Findings of fact are clearly erroneous if:

(1) the findings are not supported by substantial credible evidence;

(2) the lower court or administrative agency misapprehended the effect of the evidence; or

(3) the reviewing court has a definite and firm conviction that the lower court or administrative agency made a mistake.

Berlin v. Boedecker (1994), 268 Mont. 444, 455-56, 887 P.2d 1180, 1187. However, the district court "may not substitute its judgment" for that of STAB "as to the weight of the evidence on questions of fact." § 2-4-704(2), MCA; O'Neill, ¶ 23.[3] Moreover, a reviewing court must view findings of fact in the light most favorable to the prevailing party. Harding v. Savoy, 2004 MT 280, ¶ 20, 323 Mont. 261, ¶ 20, 100 P.3d 976. ¶ 20; Peschel Family Trust v. Colonna, 2003 MT 216, ¶ 19, 75 P.3d 793, ¶ 19. In the special case of tax appeals, the Montana Supreme Court has further stated:

> it is not a judicial function to act as an authority on taxation matters. Tax appeal boards are particularly suited for settling disputes over the appropriate valuation of a given piece of property, and the judiciary cannot interfere with that function. [Citations omitted]. Moreover, . . . assessment formulations are within the expertise of the State Tax Appeal Board and . . . its decisions [must be upheld] unless there is a clear showing of an abuse of discretion.

O'Neill, ¶ 23; MDOR v. Grouse Mtn. Development (1985), 218 Mont. 353, 355, 707 P.2d 1113, 1115.

[3] However, if the court allows supplemental evidence pursuant to § 15-2-303(5), MCA, it must then make appropriate findings of fact and conclusions of law under M.R.Civ.P. Rule 52(a). O'Neill v. MDOR (1987), 227 Mont. 226, 231, 739 P.2d 456, 459; Hi-Line Radio Fellowship v. MDOR (1987), 227 Mont. 150, 154, 737 P.2d 886, 888.

When STAB's findings of fact are uncontested on appeal, the Court must take them as stipulated facts. MDOR v. Barron (1990), 245 Mont. 100, 106, 799 P.2d 533, 536. In this case, the Department expressly stipulated to STAB FF 6-78 on pages 3 through 22 of its *Nunc Pro Tunc Factual Background, Conclusions of Law, Order, and Judicial Review* (SPT-2002-4 and SPT-2002-6). (Department's *Brief in Support of Petition for Judicial Review*, p. 2, Doc. 14). As manifest by its prayer for the Court to "summarily affirm" the STAB decision, PPLM does not contest STAB's findings of fact. (*PPLM's Brief On Judicial Review*, p. 1, Doc. 17). Accordingly, the Court hereby adopts and summarily affirms STAB FF 6-78 on pages 3 through 22 of its *Nunc Pro Tunc Factual Background, Conclusions of Law, Order, and Judicial Review* (SPT-2002-4 and SPT-2002-6).

A. STAB Jurisdiction To Adjust 2000-01 Valuations.

The first issue is whether STAB had jurisdiction to adjust the Department's valuations of PPLM's property for tax years 2000-01. The Department asserts that PPLM's original and amended complaints in SPT-2002-4 narrowly limited the scope of STAB's jurisdiction to the following issues for tax years 2000-01:

(1) whether to adjust the value of PPLM's interests in Colstrip Units 1, 2, and 3 to equalize them with PSE's Colstrip interests;

(2) whether to adjust PPLM's pollution control equipment (Class 5) for tax year 2000 for the purpose of

determining Class 13 (electric generation) property value; and

(3) whether to adjust PPLM's assessment to remove the value of intangible property from the assessed value of PPLM's Class 13 (electric generation) property.

(Department's *Petition For Judicial Review*, Doc. 1; Department's *Brief In Support*, Doc. 14). Consequently, the Department asserts that it had no notice that STAB would review its 2000-01 valuations and that the valuations were not properly at issue because PPLM failed to specifically plead them as a ground for its 2000-01 appeal.

An owner of property centrally assessed under Title 15, Chapter 23, MCA, may appeal a final decision of the Department directly to STAB. § 15-2-302(1)(a), MCA. To perfect a direct appeal, the appellant must file a complaint setting "forth the grounds for relief and the nature of relief demanded." § 15-2-302(2), MCA. Similarly, an owner of centrally assessed property who pays property taxes under protest pursuant to § 15-1-402(1), MCA, must "specify the grounds of protest" to the tax collector and to the Department. §§ 15-1-402(1)(b)(ii) and 15-1-402(c), MCA. In this case, PPLM does not assert and has not shown that it specifically pled valuation as a ground of its 2000-01 appeal.

However, a court or administrative tribunal has "jurisdiction to grant relief outside of the issues presented by the pleadings" if the "parties stipulate that other questions be considered or

the pleadings are amended to conform to the proof." H-D Irrigating, Inc. v. Kimble Properties, Inc., 2000 MT 212, ¶ 22, 301 Mont. 34, ¶ 22, 8 P.3d 95, ¶ 95; Old Fashion Baptist Church v. MDOR (1983), 206 Mont. 451, 457, 671 P.2d 625, 628. Moreover, a court or administrative tribunal also has jurisdiction to adjudicate un-pled matters raised by contention in the pretrial order. H-D Irrigating, ¶ 23; see also Harding, ¶ 67; Galetti v. Montana Power Co., 2000 MT 234, ¶ 23, 301 Mont. 314, ¶ 23, 8 P.3d 812, ¶ 23. In H-D Irrigating, the buyer of irrigation equipment under a contract for the purchase of land and irrigation equipment sued the seller to recover damages for misrepresentations in relation to the irrigation equipment. H-D Irrigating, ¶¶ 10-12. The seller counterclaimed for payments due under the contract. Id. at ¶ 1. Upon bench trial, the district court held that the seller was liable, *inter alia*, for constructive fraud based on misrepresentations related to the condition of the land rather than the irrigation equipment. H-D Irrigating, ¶¶ 13-14. On appeal, the seller asserted that the district court had no jurisdiction to award damages for misrepresentations related to the condition of the land because the complaint did not include a claim for damages related to the land. Id. at ¶ 22. The Montana Supreme Court affirmed the district court, holding that the issue was properly before the district court as a plaintiff's contention

in the pretrial order in relation to an expressly pled claim. H-D Irrigating, ¶ 23.

In contrast, Ostergren involved the Department's 1997 statewide reappraisal of class 3, 4, and 10 property. Ostergren, ¶ 2. Responding to the significant increase in appraised market value, the 1997 Legislature enacted legislation requiring the Department to phase-in market value at a 2% "rate per year of the total change in valuation between the 1996 base year (value before reappraisal or VBR) and the reappraisal value." Id. The 1996 VBR for a Missoula landfill property was $257,310. Ostergren, ¶ 3. However, in the course of the 1997 re-appraisal, the Department discovered that the owner had invested approximately $12 million in the landfill in 1995. Id. Consequently, for 1997, the Department revised the landfill's 1996 VBR upward from $257,310 to $5,281,713 and then appraised the 1997 market value as $7,398,949. Ostergren, ¶ 3.

In response, the taxpayer appealed the 1997 valuation on the asserted grounds that the 1997 valuation was erroneous and that the Department's methodology was incorrect. Ostergren, ¶ 4. The appeal "did not mention any specific objection to the property's 1996 VBR." Id. In 1999, the taxpayer similarly appealed the Department's 1999 valuation. Ostergren, ¶ 5. On appeal from the decisions of the county tax appeal board, STAB ordered revised valuations of $2,138,000 for 1997 and $2,239,000 for 1999. Id. In

noting its failure to address the accuracy of the 1996 VBR, STAB specifically stated "that it had 'not taken testimony to establish if DOR's evaluation of the VBR is accurate.'" Ostergren, ¶ 5. Upon the Department's appeal for district court review of STAB's revised valuations for 1997 and 1999, the taxpayer specifically contested the landfill's 1996 VBR for the first time. Id. at ¶ 6. However, the district court ruled that it had no jurisdiction to address the 1996 VBR issue because it "was never properly raised in front of STAB." Ostergren, ¶ 6.

Upon appeal to the Montana Supreme Court, the taxpayer asserted that the 1996 VBR was properly before STAB because:

(1) it was as an issue integral to its 1997 and 1999 appeals for reinstatement of the Department's original 1996 valuation ($257,310);

(2) the taxpayer's various arguments to STAB regarding the Department's revision of the original 1996 valuation properly placed it at issue before STAB; and

(3) STAB's decision specifically listed the 1996 VBR as a matter at issue.

Ostergren, ¶ 13. In rejecting these assertions and affirming the district court ruling, the Montana Supreme Court noted that:

(A) although the 1997 and 1999 appeals to the county tax appeal board generally stated that the appraised values were in excess of market value and that the appraisal method was incorrect, they "never specifically challenged the 1996 VBR;"

(B) the taxpayer's subsequent appeal to STAB similarly did not specifically challenge the 1996 VBR - it merely asserted that the county tax appeal board "failed to recognize the inadequacies of the valuation methods;"

(C) there was no indication that the county tax appeal board actually "reviewed the accuracy of the 1996 VBR;" and

(D) STAB's noted failure to take testimony regarding the accuracy of the 1996 values indicated that the 1996 VBR issue was not actually "in front of STAB."

Id. at 16.

In this case, in the form of a stipulated *Final Pretrial Order* signed by both parties on April 19, 2004, the parties stipulated that the "contentions of PPLM are as set forth in PPLM's Prehearing Memorandum dated April 15, 2004" and that the "[i]ssues of fact and law" before STAB "are as identified in the parties' Prehearing Memoranda dated April 15, 2004." (04-19-04 *Final Pretrial Order*, §§ II and VI, p. 1-2). PPLM's referenced prehearing memorandum is replete with assertions that the Department's 2000-01 valuations were erroneously overstated. In contrast to Ostergren, the central thrust of PPLM's prehearing memorandum was that the 2000-01 valuations were erroneously overstated based on acquisition value and that they were unequal in comparison to other Class 13 property. (*Claimant's Prehearing Memorandum*, 04-15-04, p. 1-40). Thus, as in H-D Irrigating, the parties' stipulated pretrial order squarely raised and placed the Department's 2000-01 valuations at issue before STAB, notwithstanding PPLM's characterization of the error as the Department's use of the "acquisition method."

Moreover, unlike in Ostergren, in this case STAB plainly took substantial testimony regarding the accuracy of the 2000-01 valuations, comprehensively reviewed and analyzed their accuracy, determined that they were overstated, and ultimately adjusted them downward. In light of the parties' stipulated final pretrial order and PPLM's unequivocal contentions incorporated by reference therein, the Department's claim of surprise on judicial review has no merit. Here, as in H-D Irrigating and in contrast to Ostergren, STAB had jurisdiction under the parties' stipulated final pretrial order to review and adjust the Department's valuations of PPLM's property for 2000-02.

B. STAB's 2000-01 Value Adjustments.

The second issue is whether STAB's 2000-01 valuation adjustments are erroneous. The Department asserts that STAB's adjustments are clearly erroneous because it disregarded or misapprehended the significance of PPLM's "trued-up" financial statements. (Department's *Petition For Judicial Review*, Doc. 1; Department's *Brief In Support*, Doc. 14). The term "trued-up financial statements" hereinafter refers to PPLM's independently-audited financial statements, dated January 29, 2001, as prepared for PPLM by *PriceWaterhouseCoopers, LLP* (PriceWaterhouse). (STAB Ex. J and 119).

In valuing electrical generation property, whether regulated or unregulated, the Department uses a unit assessment methodology to obtain a system valuation of the property as an entire business unit through consideration and correlation of various value indicators under the cost approach, income approach, and market approach. (STAB FF 39-40; STAB Order, p. 30-31; Day 7 Tr., p. 47-48 and 60).[4] Although it may weigh them differently depending upon the circumstances and available information in each case, the Department uniformly uses the same approach to obtain cost, income, and market indicators for regulated and unregulated electric generation property. (Day 7 Tr., p. 47-48 and 60; Day 6 Tr., p. 127).[5] To date, the Department has valued electric generation properties based on their current uses. (Day 7 Tr., p. 46 and 61-67). Accordingly, it considers the highest and best use of electric generation property to be the highest and best use of the property in its current use and regulatory environment. (Day 6 Tr., p. 113-14; Day 7 Tr., p. 61-67 and 83-85).

The cost approach generally involves:

> estimating the depreciated cost of reproducing or replacing the building and site improvements. Depreciation is deducted from this cost for loss in value caused by physical deterioration and functional or *economic obsolescence*. To

[4] See also §§ 42.22.101(30), 42.22.101(7), and 42.22.111, ARM.
[5] See also § 42.22.111, MCA.

this depreciated cost is added the estimated value of the land.

Albright v. Montana (1997), 281 Mont. 196, 199-200, 933 P.2d 815, 817 (emphasis added); see also Wayne County v. Michigan State Tax Commission (Mich. App. 2004), 682 N.W.2d 100, 121 (applied to utility property); §§ 42.22.112(2)(b) and 42.22.112(2)(d), ARM; see also Day 6 Tr., p. 119. In the context of utility property valuation, a recognized variant of the cost approach is the original/historical cost less depreciation (OCLD) method. Tennessee Gas Pipeline Co. v. Agawam Bd. of Assessors (Mass. 1998), 700 N.E.2d 818, 820; Wayne County, 682 N.W.2d at 121-125; see also § 42.22.112(2), ARM. The OCLD method reflects the net book value of utility property as derived from the company's independently-audited financial statements. (Day 6 Tr., p. 119-22; Walborn Depo., p. 65). See also Wayne County, 682 N.W.2d at 121-125. Pursuant to §§ 42.22.112(3), ARM, the Department uses the OCLD/net book value method to value electric generation property due to the limited availability of necessary information for a reliable replacement/reproduction cost analysis. (Day 6 Tr., p. 118-19; Day 7 Tr., p. 70-75 and 103). Under the OCLD/net book value method, the original cost is an allocation of the acquisition cost to the assets. (Day 6 Tr., p. 119; Day 7 Tr., p. 70 and 103). See also Wayne County, 682 N.W.2d at 107. The Department uses the audited financial statements of a utility

company to determine the OCLD/net book value of its assets. (Day 6 Tr., p. 119-22; Day Tr. 7, p. 74-75). The cost approach is most useful "where the lack of adequate market and income data preclude the reasonable application of other traditional approaches." Albright, 281 Mont. at 200, 933 P.2d at 817. The advantage of the OCLD/net book method is that the necessary source information (audited financial statements) is readily available. (Day 6 Tr., p. 120-21).

In contrast, the market approach conceptually involves:

> the compilation of sales and offerings of properties which are comparable to the property being appraised. . . The significance of this approach lies in the ability to produce estimates of value which directly reflect the attitude of the market.

Albright, 281 Mont. at 200, 933 P.2d at 817-18; Wayne County, 682 N.W.2d at 107 (applied to utility property); § 42.11.113(1), ARM. The usefulness of the market approach depends "upon the availability of comparable sales." Albright, 281 Mont. at 200, 933 P.2d at 817-18. The stock-debt approach is a variant of the market approach used by the Department to value electric utility property. (Day 6 Tr., p. 126). See also § 42.22.113, MCA. Under this approach, the Departments adds the stock price (equity component) of an acquisition with the associated debt to determine the market value of the "assets that serve that equity and debt." (Day 6 Tr., p. 126-27).

In further contrast, the income approach measures:

> the present worth of the future benefits of the property by capitalization of the net income stream over the remaining economic life of the property. This approach involves making an estimate of the "effective gross income" of a property . . . From this figure, applicable operating expenses . . . are deducted, resulting in an estimate of net income which may then be capitalized into an indication of value.

Albright, 281 Mont. at 200, 933 P.2d at 818. As similarly stated by another court, the income approach:

> measures the present value of the future benefits of property ownership by estimating the property's income stream and its resale value (reversionary interests) and then develops a capitalization rate which is used to convert the estimated future benefits into a present lump-sum value.

Wayne County, 682 N.W.2d at 128. Various income approach methods are available to the Department to determine an appropriate income indicator. See § 42.22.114, ARM. For utility property, the Department utilizes a direct capitalization/net cash flow analysis as its income approach. (Day 7 Tr., p. 110). Under this approach, the Department "normalizes" or averages historical annual income data from a utility's financial statements and then capitalizes it. (Day 6 Tr., p. 125-26; Walborn Depo., p. 127-30 and 138).

As part of the 1999 MPC divesture, PPLM not only acquired most of MPC's electric generation assets but also assumed a number of liabilities, including various power supply contracts. (STAB FF 15-18; Ex. 118, Notes 6-11; Ex. J, Notes 8-14). The original base purchase price of PPLM's MPC assets was $780,000,000. (STAB FF 8). Pursuant to the terms of the contract, the base purchase price was

adjusted down to $740,000,000 when MPC excluded Colstrip Unit 4 from the sale. (STAB FF 9). After various additions to the base purchase price, PPLM paid $757,608,137 at closing. (STAB FF 10). With the inclusion of related acquisition costs, the total amount paid by PPLM increased to $767,101,000. (STAB FF 11; STAB Ex. 118, p. 01273). In 2000, PPLM[6] reported to the IRS[7] that the "aggregate fair market value" of its MPC acquisition was $769,746,000. (STAB FF 12 and 51-52). The basis of PPLM's aggregate fair market value determination ($769,746,000) was the "roughly equivalent" figure ($767,101,000) listed in PPLM's original 1999 independently-audited financial statements prepared by PriceWaterhouse on February 25, 2000. (Day 7 Tr., p. 8 and 16; Ex. 118, p. 01273; STAB FF 11).

In late 1999 or early 2000, PPLM commissioned an independent appraiser, *Deloitte & Touche LLP* (D&T), to appraise the fair market value and provide a purchase price allocation of the acquired MPC assets for tax, accounting, and insurance purposes. (STAB FF 31 and 33; STAB Ex. HH and 115). As it did with the IRS, PPLM reported to D&T that the total purchase price of the MPC assets was $769,746,000. (STAB FF 12 and 33; STAB Ex. 115, p. 0848

[6] STAB FF 12 states that *PPL Global* filed the subject IRS Form 8594. However, STAB FF 33 indicates that PPLM made the subject filing.
[7] IRS Form 8594 is an "Asset Acquisition Statement." (STAB FF 51). The purpose of the form is to report to the IRS "how the purchase price was allocated to difference classes of assets." (Id.).

and 0855). D&T accepted that that figure without verification. (STAB Ex. 115, p. 0848 and 0855).

For 2000, based in part upon the PPLM's original independently-audited financial statements for 1999 and preliminary purchase price allocation information provided by D&T, the Department determined that the actual cost of the MPC assets was $788,683,768 -- about $19 million more than PPLM actually paid and reported to the IRS and D&T. (STAB Order, p. 11 and 31-32; STAB Ex. 118, 01273; Day 3 Tr., p. 73 and 76; Day 7 Tr., p. 103-04). The Department thus assessed PPLM as follows for 2000:

Department's 2000 Assessment	
Class 13(EGP)	$706,736,726
Class 5(PCE)	$74,629,373
Total FMV	$781,366,099

(STAB FF 41-43 and STAB Order, p.11 and 31-32). The Department based this valuation solely on the cost approach factor (OCLD/net book value) under its unit assessment methodology. (STAB FF 42; STAB Order, p. 11, 25, and 30-32; Day 7 Tr., p. 41, 102, 110-11, and 118). The Department did not consider PPLM's "trued-up" financial statements for 1999 and 2000 because they were not available until PriceWaterhouse subsequently issued them on January 29, 2001. (STAB FF 41-42; STAB Order, p. 32; STAB Ex. J).

On August 29, 2000, D&T issued its appraisal and purchase price allocation report to PPLM (STAB FF 32; STAB Ex. 115). Pursuant to IRS regulations, D&T's appraisal defined "'fair market

value' as the price at which property would change hands 'between a willing buyer and a willing seller with equity to both, neither under any compulsion to buy or sell and both fully aware of all relevant facts.'" (STAB FF 31; STAB Ex. 115, p. 0849 and 0856). In conducting its appraisal, D&T considered three approaches - market approach, cost approach, and income approach. (STAB FF 33). "Due to limited information regarding market transactions involving electric generation facilities," D&T did not determine fair market value using the market approach. (STAB FF 33; STAB Ex. 115, p. 0907). Although PPLM reported $769,746,000 as the total cost of the MPC assets, D&T determined that the fair market value of assets under its cost approach was $784,795,523. (Id.). In contrast to the OCLD/net book value method used by the Department, D&T's cost approach method used both a replacement/reproduction method involving both a "reproduction cost new" analysis, based on historical cost trending, and a "replacement cost new" analysis, based on the theoretical cost of replacement. (Day 7 Tr., p. 75; Ex. 115, p. 08794-0900). Considering the significant disparity between them, it is unclear how the Department's subsequently-determined "trued-up" cost approach valuations ($838,090,000/$840,386,189)[8] for 2000-01 reconcile with D&T's cost

[8] STAB Ex. KKKK and U.

approach valuation ($784,795,523).[9]

Under the income approach, D&T used a "discounted cash flow method" to calculate a fair market value of $800,000,000. (STAB FF 33, STAB Ex. 115, p. 0907). D&T based its income analysis on historical and projected annual production data and historical and projected prices in the energy market. (STAB Ex. 115, p. 0903). Due to its stated "difficulty in estimating inflation adjustments under the cost approach and the structure of the marketplace," D&T ultimately selected its income approach valuation of $800,000,000 as the "strongest indication" of the fair market value of the acquired MPC assets. (STAB FF 33; STAB Order, p. 32; STAB Ex. 115, p. 0907). On June 20, 2001, PPLM's Controller acknowledged the D&T appraisal "as 'a credible valuation' of PPLM's assets" and the "best indicator" of their value. (STAB FF 34).[10] The Department did not base its 2000-02 valuations on the D&T appraisal. (Day 3, Tr. 88-89).

On January 29, 2001, PriceWaterhouse issued to PPLM its independently-audited financial statements ("trued-up" financial

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[9] This issue is further muddied by the fact that, in a seemingly apples-to-oranges comparison, the Department now cites D&T's income approach valuation ($800,000,000) as support for its own 2000-01 "trued-up" cost approach valuations ($838,090,000/$840,386,189) without consideration or reconciliation of D&T's cost approach valuation ($784,795,523). See Department's *Reply Brief*, Doc. 22, p. 5 (Dept. would have valued PPLM property at $800 million for 2000-01 if it would have had PPLM's "trued-up" financials and the D&T appraisal).

[10] In contrast, PPLM proposed the following 2000 assessment on appeal to STAB:

Class 13(EGP)	$561,468,598
Class 5(PCE)	$102,890,000
Total FMV	$664,358,598

(STAB FF 44).

statements) for 1999 (revised) and 2000. (STAB Ex. J; Day 7 Tr., p. 107). As stated by PriceWaterhouse in its original 1999 report:

> . . . [t]he transaction was treated as a purchase business combination for financial reporting purposes. Assets *and liabilities assumed* have been recorded at their estimated fair market values, *and are subject to adjustment when additional information concerning asset and liability valuations is finalized.* . . .

(STAB Ex. 118, p. 01273) (emphasis added). Accordingly, in its subsequent "trued-up" financial statements issued on January 29, 2001, PriceWaterhouse clarified that:

> . . . [t]he transaction was treated as an asset purchase for financial reporting purposes. Assets acquired *and liabilities assumed* were recorded at the *preliminary estimated fair values. Some allocations* were based on studies and *valuations that were being finalized and therefore the preliminary purchase price allocation was adjusted during 2000* (see Note 13).

(STAB Ex. J, p. 014962) (emphasis added). *Inter alia,* the "trued-up statements" adjusted up the values of certain power supply contracts (assumed liabilities) and also reflected stepped-up book values resulting from the July 2000 financing transaction (sale-leaseback) wherein PPLM sold its interests in Colstrip Units 1, 2, and 3 to institutional investors for capital and then leased them back under a 36 year operating lease. (STAB Ex. J, p. 014972; Day 3 Tr., p. 8; Department's *Reply Brief*, Doc. 22, p. 4-5). PPLM certified and reported its "trued-up" financial statements to potential investors and the SEC. (Tr. Day 7, p. 153). According to the Department, PPLM's "trued-up" financial statements reflect

proper purchase accounting and most accurately account for the actual cost to PPLM of the former MPC assets by combining the purchase price with the value of the liabilities assumed by PPLM. (Tr. Day 7, p. 153; Department's *Brief*, Doc. 14, p. 8).

In March of 2001, the Department obtained copies of PPLM's "trued-up" financial statements for 1999 and 2000. (Day 7 Tr., p. 105; STAB Ex. J). Based on the "trued-up" financials statements, the Department revised its 2001 valuation of the actual cost of the MPC assets from $788,683,768 to $840,386,189. (STAB FF 42 and STAB Order, p. 11 and 31-32). This revised valuation was $70,640,189 more than the aggregate purchase price ($769,746,000) PPLM reported to the IRS in 1999 and $51,702,421 more than the Department's original valuation ($788,683,768) for 2000. According to the Department, this increase resulted from more accurate recognition of the value of the liabilities assumed from MPC *combined with* a step-up in book value resulting from the 2000 sale-leaseback transaction. (STAB Order, p. 25 and 32; Day 3 Tr., p. 8; see also Department's *Reply Brief*, Doc. 22, p. 4-5). Based upon its revised cost-approach calculation, the Department assessed PPLM for 2001 as follows:

Department's 2001 Assessment	
Class 13(EGP)	$769,234,685
Class 5(PCE)	$69,240,822
Total FMV	$838,475,507

(STAB Order, p. 11 and 31-32). Although it gave some consideration to the income approach, the Department based its 2001 assessment primarily on the cost approach. (STAB Order, p. 11 and 30-32; Day 3 Tr., p. 73, 85, and 88; Day 7 Tr., p. 161-62; Department's *Reply Brief*, Doc. 22, Ex. D).

Despite the apparent availability of historical MPC income data, the Department gave no weight to the income approach in 2000 and relatively little weight in 2001 because PPLM was the first unregulated EWG in Montana and due to insufficient income data for PPLM's use of the assets in an unregulated environment. (Day 7 Tr., p. 77-78; Department's *Reply Brief*, Doc. 22, Ex. D). The Department similarly gave little or no weight to the market approach due to limited availability of comparable transaction data. (Day 7 Tr., p. 80 and 82; Department's *Reply Brief*, Doc. 22, Ex. D). The Department found the stock-and-debt variant of the market approach similarly unreliable due to the difficulty in distinguishing the value of the subject operating assets from the aggregate value of a large corporate conglomerate. (Day 7 Tr., p. 79-81).

Under its 2002 cost approach, the Department calculated the depreciated cost of the MPC assets as $836,725,536, a reduction of $3,660,653 from 2001. (STAB Order, p. 11 and 31-32). Moreover, on the basis of two years of income history since the PPLM acquisition, the Department gave more weight (10%) to the income

approach for 2002. (STAB FF 43; Day 3 Tr., p. 88; and STAB Order, p. 33; Department's *Reply Brief*, Doc. 22, Ex. D). Giving 90% weight to the cost approach and 10% weight to the income approach, the Department assessed PPLM for 2002 as follows:

Department's 2002 Assessment	
Class 13(EGP)	$729,462,534
Class 5(PCE)	$93,401,040
Total FMV	$822,863,574

(STAB Order, p. 11 and 30-33).

On appeal, STAB found that, in applying its unit assessment methodology, the Department considered the cost approach, income approach, and market approach "by applying a correlation factor to the various approaches." (STAB Order, p. 30). In addition to considering the Department's OCLD/net book value (cost approach) analysis, STAB also considered market data in the form of the value PPLM reported to the IRS ($769,746,000) and D&T's income approach appraisal ($800,000,000). (STAB Order, p. 30-33).

STAB found that the "trued-up" net book valuations ($838,090,000/$840,386,189)[11] under the Department's cost approach reflected not only the updated book values of PPLM's assumed liabilities, but also stepped-up book values resulting from PPLM's subsequent accounting of its 2000 sale-leaseback of Colstrip Units 1, 2, and 3. Thus, STAB rejected the Department's "trued-up" assessments because it found that the sale-leaseback was merely a

[11] STAB Ex. KKKK and U.

"financing mechanism" that "added no additional value to the property." (STAB Order, p. 25 and 33).

In considering income data, STAB noted that MPC's historical income data was likely a significant consideration in the negotiated purchase price. (Id. at p. 33). However, due to a lack of detail in D&T's discounted cash flow analysis, STAB rejected D&T's income approach appraisal ($800,000,000) as an unreliable indicator of value. (STAB Order, p. 33-34; Day 7 Tr., p. 78). Based on the "very short" operating income history for PPLM and the corresponding anomalous volatility in the electric power market in 2001-02, STAB similarly found the Department's 2002 income analysis to be an unreliable indicator of value. (Id. at 25-26 and 33-34).

In considering market value indicators, STAB noted that §§ 42.20.454 and 42.20.455, ARM, contemplate consideration of a sales price or a fee appraisal as indicators of market value. (STAB Order, p. 35). Concluding that a "sales price can most definitely reflect market value," STAB found that "there is nothing to suggest that the transaction between MPC and PPLM does not meet the market value definition" of § 15-8-111, MCA. (Id.). STAB further found that the D&T appraisal supported the aggregate purchase price ($769,746,000) PPLM reported to the IRS. (STAB Order, p. 35). Therefore, concluding that the purchase price of a type of property infrequently traded in the market place "could be

the best indicator of value," STAB found that the purchase price reported by PPLM to the IRS ($769,746,000) best represented the "total value" of PPLM property for 2000-02. (Id.; *see also* Day 6 Tr., p. 115-16).

On review before this Court, the only conclusion of law implicated by the Department's assertion that STAB's 2000-01 value adjustments are erroneous is STAB's conclusion that the Department "did not properly assess PPLM's property at 100% of its market value" as required by § 15-8-111, MCA. (STAB CL 8, p. 40). The correctness of this conclusion of law turns on whether STAB's pertinent findings of fact are clearly erroneous and whether its reasoning is arbitrary or constitutes an abuse of discretion. Thus, the dispositive issue is whether STAB erred in concluding that the Department's "trued-up" valuations are inaccurate and that the purchase price was the most accurate indicator of market value.

Montana's definition of "market value" under § 15-8-111, MCA, does not preclude a determination that a recent acquisition price may best reflect the true market value of a subject property, depending upon the facts and circumstances of each case. See § 15-8-111, MCA; Albright, 281 Mont. at 206-07, 933 P.2d at 822. In this case, the Department based its 2000 assessment solely on its cost approach analysis (OCLD/net book value). By the Department's own admission and as expressly manifest in the original and

"trued-up" PriceWaterhouse statements, the Department based its original 2000 cost approach analysis on book values that were inaccurate and incomplete insofar that PPLM's original financial statements admittedly did not accurately account for the *book value* of assumed liabilities. Thus, substantial credible evidence supports STAB's conclusion that the Department's 2000 assessment was erroneous.

For 2001-02, the Department in part based its "trued-up" valuations upon stepped-up book values resulting from PPLM's accounting of the 2000 sale-leaseback transaction involving its interests in the Colstrip units. (Day 3 Tr., p. 8; STAB Ex. J, p. 014968; Department's *Reply Brief*, Doc. 22, p. 4-5) (increase in Department's "trued-up" valuations resulted from the more accurate recognition of the value of the liabilities assumed from MPC *combined with the step-up in book value resulting from the 2000 sale-leaseback transaction*). Moreover, although the Department now asserts that STAB misapprehended the effect of PPLM's "trued-up" financial statements by failing to recognize and determine the true value of the assumed liabilities, the Department stipulated, on review to this Court, to STAB FF 19 that the assumed liabilities "had the effect of *increasing the amount of consideration paid by PPLM*" and that "the precise value of the liabilities assumed by PPLM was not established during the hearing." (See Department's *Brief in Support of Petition for*

Judicial Review, p. 2, Doc. 14). Further, independent of the Department's stipulation, substantial credible evidence supports STAB's FF 19. (See Day 2 Tr. 39-43; see also Day 2 Tr., p. 53-57; Day 9 Tr., p. 59-62). Thus, based on the Department's stipulation and the underlying evidentiary support, the Court concludes that STAB did not err in concluding that the Department erred by using stepped-up values resulting from the sale-leaseback transaction.

As to STAB's 2000-01 valuation adjustments, STAB duly considered all available information and the relative reliability of that information under all three of the accepted valuation approaches. Ultimately, STAB did not disregard or misapprehend the value of PPLM's assumed liabilities, but rather, in the face of conflicting evidence, simply found the Department's evidence and analysis to be a less credible, less reliable, and less accurate indicator of value for 2000-01. Based on the fact that PPLM essentially purchased at auction a type of property infrequently traded in the market place, STAB reasonably concluded that the acquisition cost PPLM reported to the IRS ($769,746,000) was the most accurate indication of market value for 2000-02 under the circumstances of this case. Substantial credible evidence supports this conclusion. Thus, the Court further concludes that STAB's 2000-01 valuation adjustments were not clearly erroneous.

For 2002, for the same reasons, STAB again found its market value indicator more accurate and reliable than the Department's

"trued-up" cost approach analysis. Further, consistent with the Department's own limited weighting of the income approach (10%), STAB again found the income approach to be unreliable due to insufficient income data. Therefore, based on the Department's stipulation to STAB's findings of fact and the underlying evidentiary support, the Court concludes that STAB's 2000-02 valuation adjustments are not clearly erroneous and that STAB did not err in concluding that the Department failed to properly assess PPLM's property at 100% of fair market value for 2000-02 as required by § 15-8-111, MCA. Although the Court finds some merit in the Department's assertion that STAB's 2000-02 base valuations ($769,746,00) could have been reasonably adjusted up to more accurately account for the "trued-up" values of various assumed liabilities, the Department stipulated to STAB's finding that it did not determine the value of the assumed liabilities independent of the stepped-up book values resulting from the sale-leaseback transaction involving Colstrip Units 1-2. Moreover, it is not the function of the District Court to act as an authority on taxation matters and this Court may not substitute its judgment for property tax assessment formulations within STAB's field of expertise. Therefore, in regard to STAB's 2000-02 valuation adjustments, the Court concludes that STAB's conclusions of law are correct, its findings of fact are not clearly erroneous, and it did not abuse its discretion.

C. STAB'S 2001 And 2002 PCE Adjustments.

The Department next asserts that STAB abused its discretion in adjusting the Department's valuations of PPLM's Class 5 pollution control equipment (PCE). Specifically, the Department asserts that STAB abused its discretion by arbitrarily attributing a "blanket value of 10% of the total system value to PCE." (Department's *Petition For Judicial Review*, Doc. 1; Department's *Brief In Support*, Doc. 14).

PCE is identifiable property or equipment operated for the purpose of reducing or eliminating air or water pollutants. § 15-6-135(2)(a), MCA. PCE is Class 5 property taxed at 3% of market value. §§ 15-6-135(1)(b) and 15-6-125(5), MCA. The Montana Department of Environmental Quality (MDEQ) must annually certify PCE as qualifying Class 5 property. § 15-6-135(2)(a), MCA.

Based on its total systems valuations ($788,683,768, $840,386,189, and $836,725,536) for 2000-02, the Department assessed PPLM's PCE for 2000-02 as follows:

Year	Total Apport. To Counties	Class 5(PCE)	% Total App. To Counties
2000	$781,366,099	$74,629,373	9.6%
2001	$838,475,507	$69,240,822	8.3%
2002	$822,475,507	$93,401,040	11.4%
Average % Of Total Apport. To Counties:			%9.7%

(STAB FF 41-43 and 58-60; Ex. T, U, and V; STAB Order, p. 37). By informal stipulation, the Department increased the 2001-02 PCE valuations to $93,401,040. (STAB FF 59-60).

Prior to acquisition by PPLM in late 1999, MDEQ certified the subject PCE for 1999. (STAB FF 58). PPLM did not obtain a certified PCE value from MDEQ for 2000. (STAB FF 64). However, since the date of PPLM acquisition, the PCE has not significantly changed from the time last certified in 1999. (STAB FF 57). For 1999, as valued by the Department and certified by MDEQ, the value of MPC's PCE was $43,784,548. (STAB FF 58). For 2000, the Department valued PPLM's PCE at $74,629,373 by:

> calculating the proportion of value that MPC had as certified PCE compared to the total value of MPC's electric generation property, and computing a similar proportion of value for the PCE after PPLM purchased the assets.

(STAB FF 58 and 41; Ex. T). In contrast, based on the original cost of MPC's PCE as calculated by the Department ($94,000,000) and D&T's stepped-up allocations, PPLM asserted that the proper PCE valuation was the stepped-up figure of $102,890,000. (STAB FF 62). D&T's proposed PCE valuation was $92,346,554. (STAB FF 62).

Upon consideration of the evidence and various PCE valuations, STAB found that the Department's 2000-02 assessments properly "stepped-up the value" of the pollution control equipment from the value assessed to MPC at the time of acquisition by PPLM. (STAB Order, p. 37). Based on a similar ratio methodology used by

the Department and the average ratio (approximately 10%) of the Department's 2000-02 PCE assessments to the total values apportioned to the counties, STAB determined that the proper PCE value should be 10% of the total value apportioned to the counties. (STAB Order, p. 36-37). Consequently, based on its downward adjustment of the total system value of PPLM's property to $769,746,000, STAB adjusted the PCE values apportioned to the counties as follows:

Year	STAB Adjusted Class 5 (PCE)	MDOR Revised Class 5(PCE)	Difference
2000	$76,219,185	$74,629,373	$1,589,812
2001	$72,208,246	$93,401,040	($21,192,794)
2002	$69,507,392	$93,401,040	($23,893,648)

(STAB Order, p. 42).

Contrary to STAB FF 59-60, the Department now asserts that it did not stipulate to revise its 2001 PCE assessment from $69,240,822 to $93,401,040 "with no corresponding change in the underlying property." (Department's *Brief In Support*, Doc. 14, p. 10). However, on review to this Court, the Department stipulated to STAB FF 59-60 which states that the Department did in fact revise the PCE assessment to $93,401,040. (Department's *Brief in Support of Petition for Judicial Review*, p. 2, Doc. 14). Moreover, contrary to its assertion here that STAB's ratio methodology was arbitrary, the Department further stipulated on review that it

similarly used its own ratio methodology to determine its 2000 assessed value for PPLM's PCE. (STAB FF 58; Department's *Brief in Support of Petition for Judicial Review*, p. 2, Doc. 14; *see also* Day 7 Tr., p. 109-10 and 123-26). Consequently, STAB employed a reasonable PCE assessment methodology that was essentially the same type of method used by the Department, albeit with a different result. Accordingly, the Court cannot conclude that the STAB made any mistake of law, abused its discretion, or that its PCE adjustment was arbitrary or clearly erroneous. Although subject to reasonable dispute, STAB made a reasonable estimate of the value of PPLM's PCE in the face of conflicting evidence.

II - CONSTITUTIONAL EQUAL PROTECTION

PPLM further asserts that Montana has unequally assessed its property in relation to the same or similar electric generation property owned by PSE and Avista thereby resulting in a disparate tax burden in violation of the equal protection clauses of the Fourteenth Amendment of the U.S. Constitution and Mont. Const. art. II, § 4. (PPLM's *Brief On Judicial Review*, p. 14 and 16). PPLM more specifically claims that Montana has violated equal protection standards by: (1) assessing Class 13 electric generation property on the basis of value in use; (2) failing to obtain "seasonable attainment" of equality between PPLM and PSE/Avista; and (3) imposing a disproportionate tax burden on

PPLM. *Inter alia*, PPLM asserts the following facts in support of this claim:

(1) prior to acquisition by PPLM, Montana assessed the subject MPC properties at a market value of $504 million for 1999. In 2000, after acquisition by PPLM and without any significant change in assets or physical operations, Montana assessed the same properties at market values of $788 million, $900 million, and $915 million for 2000-02;

(2) prior to the PPLM acquisition, the MPC assets constituted approximately 30% of the assessed market value for electric generation property in Montana. Following the PPLM acquisition and reassessment in 2000-02, the assessed market value of the same assets increased to approximately 50% of the assessed market value for electric generation property in Montana;

(3) coincident to the significant increase in the assessed value of PPLM's property in 2000-02, Montana did not correspondingly increase the assessed value of electric generation assets operated in Montana by *PSE* and *Avista*;

(4) Montana assessed PPLM's undivided 50% interest in Colstrip Units 1 and 2 at a significantly higher market value than *PSE's* undivided 50% interest in the exact same assets and operation; and

(5) based on comparable megawatt production capacities, Montana has increased its assessment of PPLM's hydroelectric production assets (dams) from 190% of the assessed market value of *Avista's* hydroelectric assets to a relative percentage in excess of 500% of the value assessed to *Avista*.

Although PPLM's factual assertions are based on the Department's assessed valuations for 2000-02 rather than STAB's adjusted valuations, PPLM asserts that STAB's adjusted valuations suffer from the same constitutional defects.

The Department acknowledges that, upon acquisition from MPC, the assessed market value and resulting property tax burden on PPLM's electric generation assets has significantly increased in relation to the other electric generation properties in Montana. However, the Department asserts that the valuation disparity is simply the lawful result of the fact that PPLM's electric generation assets have a significantly higher market value as unregulated EWG assets than their value as regulated utility assets when owned by MPC. Thus, the Department asserts that it has lawfully assessed and equalized the value of electric generation property operated by PPLM, PSE, and Avista in accordance with their respective fair market values. (Department's *Reply Brief*, Doc. 22).

The Fourteenth Amendment to the U.S. Constitution and Article II of the Montana Constitution similarly provide that "[n]o person shall be denied equal protection of the laws." U.S. Const. art. XIV, § 1; Mont. Const. art. II, § 4. The Montana Constitution further provides that the State "shall appraise, assess, and equalize the valuation of property . . . in the manner provided by law." Mont. Const. art. VIII, § 3. As applicable here, the equalization requirement of Mont. Const. art. VIII, § 3, affords no greater protection to PPLM than the equal protection guarantees of the U.S. and Montana Constitutions. See Kottel v. Montana, 2002 MT 278, ¶¶ 39-45, 312 Mont. 387, ¶¶ 39-45, 60 P.3d 403, ¶¶ 39-45.

Thus, whether characterized as a constitutional equalization issue or an equal protection issue, equal protection standards govern PPLM's constitutional claim in this case. See Kottel, ¶¶ 39-45; Roosevelt v. MDOR, 1999 MT 30, ¶¶ 24-41, 293 Mont. 240, ¶¶ 24-41, 975 P.2d 295, ¶ 24-41.

In analyzing an equal protection claim, the court must determine:

(1) whether government action has resulted in a different classification of, or discrimination among, similarly situated individuals;

(2) if so, what is the proper level of constitutional scrutiny for the type of government classification or discrimination at issue; and

(3) whether the government rationale for the classification or discrimination satisfies the applicable level of scrutiny.

See Kottel, ¶¶ 47-56; Roosevelt, ¶ 27; Nordlinger v. Hahn (U.S. 1992), 505 U.S. 1, 10, 112 S.Ct. 2326, 2331-32.[12] Accordingly, the first issue is whether government action has resulted in a different classification of, or discrimination among, similarly situated individuals. "Appraisal or valuation is the act of ascertaining the market value of taxable property . . . and deals with the individual aspects of specific property." Hanley v. MDOR (1983), 207 Mont. 302, 308, 673 P.2d 1257, 1260. In contrast, equalization "refers to adjustments made between class, county,

[12] PPLM does not assert that Montana's equal protection guarantee provides any greater protection than that of the U.S. Constitution.

and individual property values . . . and is a much broader and more amorphous" concept. Id. Accordingly, consistent with constitutional equal protection and property tax equalization standards, "it is the policy of the State of Montana to provide for equitable assessment of taxable property . . . and to provide for periodic revaluation . . . in a manner that is fair to all taxpayers." § 15-7-131, MCA.

The Department annually re-appraises and assesses all electric generation property in Montana. §§ 15-23-101(2) and 15-8-112, MCA; § 42.22.1315(1), MCA. Moreover, the Department must assess all properties at 100% of market value. § 15-8-111, MCA. For purposes of property taxation, "market value" means:

> the value at which property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts.

§ 15-8-111(2)(a), MCA. In pertinent part, Montana law further requires the Department to "adjust and equalize the valuation of property" between individual taxpayers in the same classes of taxable property and to "do all things necessary to secure a fair, just, and equitable valuation of all taxable property" between individual taxpayers in the same classes of taxable property. § 15-9-101(1), MCA. Accordingly, the Department must use:

> the same method of appraisal and assessment . . . to the end that *comparable property with similar true market values*

> . . . shall have substantially equal taxable values at the end of each cyclical revaluation.

§ 15-7-112, MCA (emphasis added). The term "comparable property" means property that:

> (1) has similar use, function, and utility;
>
> (2) is influenced by the *same set of economic trends* and physical, *governmental*, and social factors; *and*
>
> (3) has the potential of a similar highest and best use.

§ 15-1-101(1)(e), MCA (emphasis added). Together, Mont. Const. art. VIII, § 3, and the above-referenced statutes require:

> standardized appraisal methods . . . with the ultimate goal that the valuation of taxable property be equalized among . . . individual taxpayers, and that once equalized, that property be assessed for tax purposes at 100% of market value . . .

Roosevelt, ¶ 23.

As recognized by the Montana Supreme Court in 1997, the term "same method" as used in § 15-7-112, MCA:

> does not refer to any single approach; rather, the term "method" *refers to a consistent process for arriving at market value, the details of which may vary* from place to place, *depending on available data*, and which will necessarily include a number of different approaches -- *e.g.*, the market data approach, the income approach, the cost approach--or some combination of these approaches, *depending on the market* in the area where appraisals occur.

Albright, 281 Mont. at 208-09, 933 P.2d at 823 (emphasis added); see also §§ 42.22.111, 42.22.101(7), 42.22.1309, 42.22.112, 42.22.113, 42.22.114, ARM. Thus, in accordance with the equalization requirement of Mont. Const. art. VIII, § 3, and § 15-

7-112, MCA, "a number of different approaches" may be used "to appraise, assess, *and equalize* the valuation of property." Albright, 281 Mont. at 212, 933 P.2d at 825 (emphasis added).

PPLM and PSE each own an undivided 50% interest in Colstrip Units 1 and 2. (STAB FF 65; *see also* STAB FF 13-14). During tax years 2000-02, PSE's Montana assets were regulated, rate-based utility assets, subject to regulation by the Washington Public Utility Commission. (STAB FF 65). During 2000-02, PSE used its Montana assets exclusively for the purpose of producing power for rate-regulated customers. (STAB FF 65). PSE does not own or operate any electric generation assets operated as or by an unregulated EWG in Montana. (STAB FF 65).

Under its current regulated status, PSE must utilize all of its power share from Colstrip Units 1 and 2 to supply rate-regulated power to rate-based retail customers. (STAB FF 68-69). Under this regulated status, PSE may sell excess power from its Colstrip Units in the wholesale markets, but must credit any proceeds from the sale of excess power to the benefit of rate-regulated customers to reduce their utility rates. (STAB FF 68-69). PSE may not sell excess power to increase its net income. (STAB FF 68-69). Notwithstanding the right to sell excess power on the wholesale market to benefit rate-regulated customers, PSE does not compete in the wholesale market in any meaningful respect. (STAB FF 69). Although it may sell excess power on the wholesale

market to benefit rate-regulated customers, PSE does not have sufficient generation output to satisfy all of its rate-regulated retail demands. (STAB FF 70). Consequently, for tax years 2000-02, PSE had to purchase power from PPLM for resale to PSE customers. (STAB FF 70).

Avista is an energy company engaged in the production, transmission, and distribution of hydroelectric power. (STAB FF 71). The Noxon Rapids Dam, located on the Clark Fork River in northeastern Montana, is Avista's largest hydroelectric generator with a generating capacity of 554 megawatts. (STAB FF 71). The Noxon Rapids Dam generates 70% of the total capacity of Avista's Clark Fork generating assets. (STAB FF 71). In contrast, PPLM's eleven geographically dispersed hydroelectric dams have a total generating capacity of 577 megawatts. (STAB FF 72). Avista's Montana hydroelectric generation assets generate an annual average of 3,371 megawatt-hours of electricity per megawatt of capacity. (STAB FF 72). In contrast, PPLM's hydroelectric generation assets produce an annual average of 6,489 megawatt hours of electricity per megawatt of capacity. (STAB FF 72).

During tax years 2000-02, Avista operated its Noxon Rapids facility as a regulated, rate-based utility subject to regulation by the Washington Public Service Commission. (STAB FF 73). This regulated status required Avista to generate power for supply to rate-regulated customers. (STAB FF 73-74). Avista does not operate

or generate power in Montana as an unregulated EWG. (STAB FF 73). Avista may sell excess power, but must credit the proceeds to benefit its rate-regulated customers and may not sell excess power to increase its net income. (STAB FF 75). Avista does not sell excess power at wholesale and does not use Montana-generated electricity to compete in the wholesale market in any meaningful respect. (STAB FF 75). Avista's Montana electric output is fully committed to satisfy the rate-regulated retail requirements of its rate-based customers. (STAB FF 75). Like PSE, Avista does not have sufficient capacity to satisfy all of its rate-regulated retail obligations and therefore must purchase power from other providers for resale to its rate-regulated customers. (STAB FF 76).

In contrast to PSE and Avista, PPLM has never operated its Montana electric generation assets as a rate-based utility subject to regulation by a state public utility regulatory agency. (STAB FF 66). The negotiated MPC-PPLM purchase agreement was expressly contingent upon PPLM obtaining unregulated EWG status from FERC. (STAB FF 20). Although still regulated to a limited extent by FERC under the federal law that deregulated the power industry, EWGs are exempt from regulation by state public utility regulatory agencies. (STAB FF 20).[13] Thus, although it may not sell directly to retail customers, an EWG may sell power on the wholesale market

[13] See Part II, Federal Power Act, 16 U.S.C. §§ 824-824m; Title 69, Chapter 8, MCA (Montana Electric Utility Restructuring Act), infra.

at market rates. (STAB FF 22). Consequently, electric generation assets operated as unregulated EWGs operate in a substantially different regulatory and economic environment than similar electric generation assets that continue to operate as regulated, rate-based utility assets subject to regulation by a state public utility regulatory agency. (STAB FF 67 and 20; Day 7 Tr. p. 52-53, 66-67, 82-85). Under the terms of the MPC-PPLM purchase agreement, PPLM would not have completed the purchase if FERC did not grant it EWG status. (STAB FF 20-21). FERC granted EWG status to PPLM in June of 1999. (STAB FF 21). Thus, although PPLM has operated the former MPC assets in the same physical manner and for the same general purpose (electric generation) as MPC operated them before deregulation of the power industry in Montana, PPLM has operated exclusively as an unregulated EWG authorized to sell power at market rates on the wholesale market. (STAB FF 22-23 and 66). Accordingly, for tax years 2000-02, PPLM was considerably more profitable than PSE and Avista. (STAB FF 77).

PPLM essentially asserts that the Department's 2000-02 valuations and STAB's adjusted valuations violate equal protection by arbitrarily discriminating against PPLM on the basis of a "value in use" distinction in the application of the generally accepted value indicators (cost approach, market approach, and income approach). PPLM thus asserts that this distinction effectively creates two classifications of Class 13 property --

regulated electric generation property (PSE and Avista) and unregulated electric generation property (PPLM). In analyzing PPLM's equal protection claim, the Court must first determine whether, as applicable in this case, Montana is actually discriminating between similarly situated taxpayers, *i.e.*, whether Montana has created different classifications of Class 13 electric generation property.

To value PPLM's property for 2000-02, the Department primarily used a cost approach based on PPLM's net book value and also considered to a lesser extent a direct capitalization income approach. (Day 3 Tr., p. 73, 85, and 88; Department's *Reply Brief*, Doc. 22, Ex. D). As found by STAB in its uncontested findings of fact, the Department "utilized the same methodology and approach in appraising" the electric generation facilities of PPLM, PSE, and Avista. (STAB FF 78 and 39-40; Day 3 Tr., p. 73, 85, and 88; Day 6 Tr., p. 127; Day 7 Tr., p. 47-48 and 60; Walborn Depo., p. 151-52; STAB Order, p. 30-31; Department's *Reply Brief*, Doc. 22, Ex. D).[14] Thus, as manifest by the Department's 2000-02 appraisals of PPLM, PPLM's 2000 D&T appraisal, and the Department's 2000-02 assessments of PSE and Avista, the differences in the 2000-02 valuations between PPLM and PSE/Avista is not due to different valuation methodology or approaches, but rather, due to the effect of different regulatory and economic circumstances on value

[14] See also §§ 42.22.101(30), 42.22.101(7), and 42.22.111, ARM.

indicators within the traditional valuation approaches, *i.e.*, differences in relative profit potentials, market factors, and the accuracy and reliability of available information for each of the properties in their respective regulatory environments.

In adjusting the Department's PPLM valuations, STAB similarly used the same unit valuation methodology and considered the same valuation approaches (cost, market, and income) within that methodology. (*See* STAB Order, p. 30-35). The difference between the Department and STAB valuations is that, in the face of conflicting evidence, STAB found a market indicator to be the most reliable indicator of the value of PPLM's property for 2000-02. (Id.). Although the Department and STAB disagreed as to which value indicators were the most accurate and reliable, they both based their valuations on the same type of information - values originally or subsequently booked and reported by PPLM. Contrary to PPLM's assertion, and as similarly found by STAB, neither the Department methodology nor the STAB methodology constitutes or equates with a simple acquisition cost methodology because they both carefully considered and weighed the accuracy and reliability of all three of the standard value indicators (cost, market, and income) based upon available information. Thus, irrespective of their differing views and results, the Department and STAB valuations were the result of a uniform and reasonable appraisal methodology which considered all relevant and available

information pertinent to each property. See Albright, 281 Mont. at 213, 933 P.2d at 823.[15] Therefore, despite PPLM's creative mischaracterization, the Department and STAB did not apply different valuation methods to PPLM and have not effectively created two classifications of Class 13 electric generation property in Montana.

Moreover, equal protection and equalization standards require only that that *comparable property with similar true market values* have substantially equal taxable values at the end of each cyclical revaluation. See §§ 15-7-112 and 15-1-101(1)(e), MCA; Roosevelt, ¶¶ 19-23; Albright, 281 Mont. at 213, 933 P.2d at 823; see also Nordlinger, 505 U.S. at 10, 112 S.Ct. at 2331 (equal protection does not bar classifications - only requires government to similarly treat those who are in all relevant respects alike). In this context, the term "comparable property" means property that:

(1) has similar use, function, and utility;

(2) is influenced by the *same set of economic trends* and physical, *governmental*, and social factors; *and*

[15] Note further that the Montana Supreme Court has recognized that "the Department's method of assessing property and estimating market values is by no means perfect, and will occasionally miss the mark when it comes to the Constitution's goal of equalizing property valuation. However, perfection in this field is, for all practical purposes, unattainable due to the logical and historical preference[s] . . . and the occasional lack of market data. Nonetheless, we conclude that the Department's interdisciplinary method--which utilizes the market data approach, the income approach, the cost approach, or some combination of these approaches -- is a reasonable attempt to equalize appraisal of real property throughout the State and that it comports with the most modern and accurate appraisal practices available. Albright, 281 Mont. at 213, 933 P.2d at 823.

(3) has the potential of a similar highest and best use. § 15-1-101(1)(e), MCA (emphasis added). In this case, the jointly-owned Colstrip Units 1-2 are obviously the same property, with the same function, and same physical utility. Likewise, the hydroelectric generation facilities of PPLM and Avista unquestionably have similar use, function, and physical utility. Moreover, subject to federal and state regulatory approval,[16] PSE and Avista could conceivably similarly convert their regulated generation assets for use as unregulated EWG assets. (*See, e.g.*, Day 1 Tr., p. 152-55). Thus, the Montana electric generation assets of PPLM and PSE/Avista *at least potentially* have the same highest and best economic use.

However, under the regulatory status quo, the electric generation properties of PPLM and PSE/Avista are not currently subject to, and influenced by, the same set of regulatory and economic restrictions, factors, and environment. PPLM and PSE/Avista operate in substantially different regulatory and economic environments. As an EWG, PPLM may sell an unlimited amount of power on the wholesale market for profit at market rates. In the regulated environment in which they operate, PSE and Avista may not profit above the reasonable rate of return that state regulatory agencies authorize them to recover on their

[16] See Part II, Federal Power Act, 16 U.S.C. §§ 824-824m; Title 69, Chapter 8, MCA (Montana Electric Utility Restructuring Act), infra.

investments. (Day 7 Tr., p. 82-84). Consequently, PPLM's Montana electric generation assets have been substantially more profitable and have substantially more profit-potential than those of PSE/Avista under the regulatory status quo.

Contrary to PPLM's assertion that Montana law does not allow consideration of comparative regulatory status and resulting economic effect in the valuation of electric generation properties, Montana law not only authorizes, *but requires*, the Department and STAB to consider the effect of "economic trends," "government factors," economic obsolescence, and government restrictions on the relative value of property in Montana. See Grouse Mtn., 218 Mont. at 357-58, 707 P.2d at 1117 (effect of government use restrictions); see also §§ 15-7-112, 15-1-101(1)(e)(ii), and 15-8-111, MCA; Albright, 281 Mont. at 199-200, 933 P.2d at 817 (consideration of economic obsolescence); § 42.22.101(8), ARM; see similarly Tennessee Gas, 700 N.E.2d at 820 (must consider effect of regulation on value of electric generation property). Similarly, consistent with the evidence in this case, a number of other courts have specifically recognized that, in the wake of deregulation of the energy industry, electric generation properties operating as unregulated EWGs are more valuable to potential purchasers because they have greater revenue potential than regulated electric generation property. See Tennessee Gas, 700 N.E.2d at 820-21 (value of electric generation

property limited while regulated); Wayne County, 682 N.W.2d 100, 132 (there is no doubt that regulation affects the value of utility companies by controlling their rate of return); see also PP&L, Inc. v. Pennsylvania (Pa. 2003), 828 A.2d 1181. The PSE/Avista properties therefore do not have the same highest and best use as the PPLM properties in their current regulatory environment. Consequently, based upon comparative regulatory status and resulting differences in profit potential and market value, PPLM's unregulated EWG property and PSE's/Avista's regulated utility property are not comparable properties for purposes of §§ 15-7-112, 15-1-101(1)(e), and 15-8-111, MCA, and are thus not similarly situated properties for purposes of constitutional equal protection. Thus, if all Class 13 electric generation property is assessed at 100% of market value under prevailing regulatory and economic conditions, assessment of PPLM's unregulated electric generation assets at a significantly higher value than the otherwise similar regulated generation assets of PSE/Avista on the basis of market value disparities resulting from differences in regulatory status does not effectively result in different classifications of, or discrimination among, similarly situated Class 13 electric generators.

However, even if, *arguendo,* the Court concluded that the disparate valuations of PPLM and PSE/Avista based on differences

in regulatory status result in different classifications of, or discrimination among, similarly situated Class 13 taxpayers in this case, a rational basis would still exist for the classification or discrimination. Under the equal protection analysis, government classification of, or discrimination among, similary situated individuals is lawful if justified under the appropriate level of constitutional scrutiny. Kottel, ¶¶ 47-56; Roosevelt, ¶ 27; McGowan v. Maryland (U.S. 1961), 366 U.S. 420, 425-26, 81 S.Ct. 1101, 1105. The proper level of constitutional scrutiny for equal protection claims involving property tax classifications is the lowest level of scrutiny - the rational basis test. Kottel, ¶¶ 50-56; Nordlinger, 505 U.S. at 10-11; 112 S.Ct. at 2331-32. Under the rational basis test, a government classification or discrimination that results in unequal burdens is permissible if based on reasonable and substantial grounds that actually distinguish one class from another. Kottel, ¶ 54. For purposes of equal protection, government action has a rational basis if it "rationally furthers a legitimate state interest." Nordlinger, 505 U.S. at 11; 112 S.Ct. at 2332. Government action generally furthers a legitimate state interest if:

(1) there is a plausible policy reason for the classification;

(2) the government decisionmaker may have rationally considered the legislative facts on which the classification is apparently based; and

(3) the relationship of the classification to its goal is not so attenuated as to render the distinction arbitrary or irrational.

Fitzgerald v. Racing Assoc. of Central Iowa (U.S. 2003), 539 U.S. 103, 107, 123 S.Ct. 2156, 2159; Nordlinger, 505 U.S. at 11; 112 S.Ct. at 2332.

As manifest in § 15-8-111(1), MCA, the State of Montana has a legitimate state interest in taxing all property, including electric generation property, at 100% of fair market value upon consideration of all relevant facts and circumstances. To this end, pursuant to §§ 15-8-111, 15-7-112, and 15-1-101(1)(e), MCA, the Legislature has authorized and directed the Department and STAB to consider and make valuation distinctions, based on individual characteristics and circumstances, *among properties within the same statutory tax classes*[17] in order to appraise and equalize property values within each class. Ostergren, ¶¶ 19-21 (equalization may be based upon divergent circumstances of otherwise similarly situated taxpayers); Albright, 281 Mont. at 208-13, 933 P.2d at 823-26. Accordingly, Montana law requires the Department and STAB to consider the effect of the regulatory environment and resulting economic effect in valuing the electric generation properties in Montana. See Grouse Mtn., 218 Mont. at 357-58, 707 P.2d at 1117; §§ 15-7-112, 15-1-101(1)(e)(ii), and 15-

[17] See §§ 15-6-131 through 15-6-157, MCA (definitions of statutory Classes 1-14).

8-111, MCA; § 42.22.101(8), ARM; see also Albright, 281 Mont. at 199-200, 933 P.2d at 817 (consideration of economic obsolescence); see similarly Tennessee Gas, 700 N.E.2d at 820 (effect of regulation on value of electric generation property must be considered).

In this case, irrespective of their differing views as to the most reliable value indicator based on available information, the Department directly, and STAB indirectly, based their valuations of PPLM's electric generation property on the actual fair market value of the property in the unregulated environment in which it was acquired and operates, as reflected in the actual purchase price of the open market transaction and the net book value derived from PPLM's independently-audited financial statements. Using the same methodology, the Department valued the PSE and Avista properties based on net book values derived from their respective financial statements. (STAB FF 78; Day 6 Tr., p. 127; Day 7 Tr., p. 47-48; Walborn Depo., p. 151-52). Thus, if net book value accurately reflects the market value of the electric generation property of PSE and Avista *in the regulated environment in which they operate*, a rational basis exists under Montana law for the resulting disparity in property tax burden between the unregulated PPLM property and the regulated PSE/Avista property.

As a result, the lynchpin of PPLM's equal protection claim is whether the Department's net book valuations of PSE and Avista

accurately reflect their market value *in the regulated environment in which they operate*. As a preliminary matter, PPLM has the burden of proving that the Department has under-valued the electric generation property of PSE and Avista in relation to § 15-8-111, MCA (100% market value requirement). See Farmers Union, 272 Mont. at 476, 901 P.2d at 564; MDOR v. STAB-Countryside Village (1980), 188 Mont. 244, 251, 613 P.2d 691, 695-96; Northwest Land & Develop. of Montana, Inc. v. State Tax Appeal Board (1983), 203 Mont. 313, 316, 661 P.2d 44, 46. Although PPLM relies on the tax burden disparity between itself and PSE/Avista/MPC, it has not overcome the evidentiary showing by the Department that it utilized the same unit assessment methodology and incorporated valuation approaches in appraising the electric generation facilities of MPC, PSE, Avista, and PPLM. (STAB FF 78 and 39-40; Day 3 Tr., p. 73, 85, and 88; Day 6 Tr., p. 127; Day 7 Tr., p. 47-48 and 60; Walborn Depo., p. 151-52; STAB Order, p. 30-31; Department's *Reply Brief*, Doc. 22, Ex. D). Although it considered the cost, market, and income approaches within this methodology, the Department primarily relied on the net book value cost approach for all electric generation property in Montana in 2000-02. (Walborn Depo., p. 151-52; Day 3 Tr., p. 73, 85, and 88; Department's *Reply Brief*, Doc. 22, Ex. D).

Under its cost approach, the Department determines the net book value of electric generation property from each company's

independently-audited financial statements. (Day 6 Tr., p. 119-22; Walborn Depo., p. 65). The Department's stock-debt variant of the market approach is also based, at least in part, on information (stock price/equity and associated debt) derived from a company's independently-audited financial statements. (Day 6 Tr., p. 126-27). Moreover, the Department's income approach (direct capitalization/net cash flow analysis) is similarly based upon income data from each company's independently-audited financial statements. (Day 6 Tr., p. 125-26; Day 7 Tr., p. 110).

The regulated status of PSE and Avista limits their profitability to a reasonable rate of return approved by a state regulatory agency to allow them to recover on their respective investments. (Day 7 Tr., p. 82-84). This regulated rate of return or profit limitation is reflected in their audited balance sheets and financial statements and thus in any net book value or cash flow analysis based thereon. (Day 7 Tr., p. 83-84 and 93-94). Accordingly, because the Department's cost, market, and income approaches are based on the independently-audited financial statements of PPLM, PSE, Avista, and previously, MPC, the effect of regulation and the resulting profit-limitation on market value is reflected in the Department's valuations of PSE and Avista and contrasted in that of PPLM. (Day 6 Tr., p. 131-32). In either event, each company's independently-audited financial statements are *generally* a reliable and accurate reflection of value because

they are independently-audited in accordance with generally accepted accounting principles and because they are the statement of value that the utility companies report to their respective shareholders and to the federal and state governments for taxation, securities regulation, and rate regulation purposes. (*E.g.*, Walborn Depo., p. 64-65, 75, 138-39).

In *dicta* noting that it had no jurisdiction to address PPLM's constitutional equal protection claim, STAB gratuitously speculated that:

> . . . Montana Class 13 property has been primarily cost-based. While there is a discussion of a "correlation of value," the practical effect is that the original or historical cost of the utility property is depreciated, so that the value diminishes each year. There is no attempt to trend or index this amount to reflect price levels in the macro economy. Without such a device or some other methodology, *one would expect* that the assessments have the potential to move away from actual market values. *This may be one reason why* the facilities owned by Montana Power in 1999 were assessed by DOR at 504 million; but when those exact same facilities were sold in the open market to PPLM they obtained a value of $769 million.
>
> This discrepancy in valuation can be seen most vividly in Colstrip Units 1 and 2[, co-owned on a 50%/50% basis by unregulated PPLM and regulated PSE]. . . . While DOR maintains that both properties are assessed using the "cost" approach to value, the fact is that one cost approach uses historical costs depreciated (PSE), and the other uses cost based upon purchase price (PPLM). It strains reason to argue that both properties are assessed by the same method, when the results are so dramatically different.

(STAB Order, p. 38-39). Beyond being gratuitous and speculative

dicta, STAB's suggestion that the Department used different cost approaches for regulated and unregulated property squarely contradicts STAB's own uncontested finding of fact and the underlying supporting evidence. (*See* STAB FF 78; Day 6 Tr., p. 127; Day 7 Tr., p. 47-48). Moreover, STAB's narrow focus on the resulting tax burden disparity fails to recognize the actual reason for the disparity. The reason for the disparity is not that the Department used one cost approach (historical OCLD/net book value) for PSE/Avista and another (acquisition cost) for PPLM - as applied in this case, both approaches are the same approach based on respective current net book values as manifest in the independently-audited financial statements of the companies. (STAB FF 78; Day 6 Tr., p. 127; Day 7 Tr., p. 47-48; Walborn Depo., p. 151-52). The reason that the same cost approach method yields dramatically disparate results in this case is that the otherwise similar properties actually have dramatically different market values based on the difference in regulatory status and resulting economic effect. (*See, e.g.*, Day 7 Tr., p. 82-85). *Inter alia*, this conclusion is manifest by: (1) the actual negotiated purchase price of the former MPC assets; (2) the fact that PPLM expressly conditioned its purchase obligation on obtaining unregulated EWG

status; and (3) the accordingly disparate post-acquisition values booked by PPLM. (*See, e.g.*, Day 7 Tr., p. 83).[18]

STAB's suggestion, and PPLM's assertion, that the Department's failure to trend or index the net book value of regulated properties "to reflect price levels in the macro economy" results in below market value valuations of regulated property is similarly without merit. The Department admittedly does not trend or index original costs back to current costs under its net book value cost approach. (Day 7 Tr., p. 72-75). However, STAB and PPLM ignore the reason why. The Department does not trend original costs back to current costs because the net book values reflected in a company's independently-audited financial statements accurately reflect the market value of a regulated company's electric generation property *under its prevailing regulatory status* as reported to shareholders and the federal and state governments for taxation, securities regulation, and rate regulation purposes. (Walborn Depo., p. 64-65; Day 7. Tr., p. 74-75). As additional support for this rationale, the Department presented credible testimony that correlation of the net book value cost approach and the income approach will account for income fluctuations and that, over time, the cost approach and

[18] Similarly illuminating is the fact that PPLM's 2000 attempt to purchase the rest of the outstanding ownership interests in the former MPC Colstrip units from PSE and *PortlandGen* fell-through when the Washington and Oregon state utility commissions required PSE and *PortlandGen* to allocate 100% of the gain from the sale to their rate-regulated customers rather than to shareholders as profit. (Day 1 Tr., p. 152-55).

income approach valuations will converge and be in substantial equilibrium. (Walborn Depo., p. 64-64). Thus, PPLM has not shown that the Department's failure to trend the net book value of regulated properties results in undervaluation of PSE and Avista.

Finally, in the form of its "highest and best use" argument, PPLM further asserts that, in the wake of deregulation, the highest and best potential use of all electric generation property in Montana is as unregulated EWG property, and therefore, § 15-8-111, MCA, requires Montana to appraise all electric generation properties at the value they would exchange hands as such, irrespective of their current regulated status. Aside from tacitly supporting the Department's position that unregulated EWG status makes electric generation property more valuable than regulated generation assets, this argument conveniently overlooks the fact, as clearly manifest in the conditional MPC-PPLM transaction, that regulated electric generation assets do not have a market value significantly greater than their current book value *unless and until* they can be operated as unregulated EWG assets. Moreover, regulated electric generation assets cannot be converted to

unregulated EWG assets without federal and state regulatory approval. (*E.g.*, Day 7 Tr., p. 85; Day 1 Tr., p. 152-55).[19] Consequently, PPLM has not shown that the Department failed to assess the electric generation properties of PSE and Avista at 100% of fair market value in the regulated environment in which they operate. PPLM has shown only that the former MPC assets are subject to a significantly higher tax burden since converting from regulated to unregulated electric generation property. Thus, Montana's consideration of relative regulatory status and resulting economic effect in the assessment of Class 13 electric generation property rationally furthers the State's legitimate interest in assessing all taxable property at 100% of market value in accordance with § 15-8-111, MCA.

PPLM further analogizes this case to property tax assessments struck down on equal protection grounds in Allegheny Pittsburgh Coal Co. v. Webster Co. Commission (U.S. 1989), 488 U.S. 336, 109 S.Ct. 633, Roosevelt, and Barron. In Allegheny, with some minor adjustment, the West Virginia county assessor annually assessed coal production property at the amount at which the property last sold. Allegheny, 488 U.S. at 338, 109 S.Ct. at 635. As a result of this assessment policy, new purchasers of coal production property

[19] See also Part II, Federal Power Act, 16 U.S.C. §§ 824-824m; Title 69, Chapter 8, MCA (Montana Electric Utility Restructuring Act), infra.

were systematically assessed at values that were dramatically disproportionate to otherwise similar coal production property with the only difference being the date of transfer/sale of the properties. Id. at 339-41, 109 S.Ct. at 637. As a threshold matter, the U.S. Supreme Court noted that the use of two methods "to assess property in the same class" in is not a *per se* violation of equal protection - the "Equal Protection Clause applies only to taxation which in fact bears unequally on persons or property of the same class."[20] Allegheny, 488 U.S. at 343, 109 S.Ct. at 637. Finding that the subject assessment policy treated comparable property differently, the Supreme Court further noted that disparate property tax treatment does not violate equal protection if rationally related to a legitimate state interest. Id. at 344-45, 109 S.Ct. at 638-39. Further finding that the subject assessment policy was not rationally related to the asserted state interest of assessing all properties "at true current value," the U.S. Supreme Court held that the subject assessment policy violated the Equal Protection Clause of the Fourteenth Amendment. Allegheny, 488 U.S. at 343-46, 109 S.Ct. at 637-39.[21]

[20] PPLM artfully attempts to apply this "class" reference to Montana's statutory tax classifications. However, the context of this usage plainly indicates that the U.S. Supreme Court was referring to "class" in the constitutional sense, *i.e.*, similar or comparable irrespective of statutory tax classification. See Allegheny, 488 U.S. at 343-44, 109 S.Ct. at 637-38.

Similarly, in Roosevelt, in an attempt to soften the tax impact of general increases in the appraised value resulting from the 1996 re-appraisal of Class 4 property, the Montana Legislature mandated a phase-in of the appreciated change in value at the rate of 2% per year. Roosevelt, ¶¶ 21-24. The 2% phase-in effectively benefited Class 4 properties that appreciated in value but resulted in above-market value assessment of Class 4 properties that had depreciated in value upon re-appraisal. Roosevelt, ¶ 24. As in Allegheny, the Montana Supreme Court held that, as applied to the Class 4 plaintiff whose property had depreciated upon re-appraisal, the 2% phase-in provision resulted in unequal treatment of similarly-situated Class 4 properties. Roosevelt, ¶¶ 32-41. In assessing the rationale for this disparate treatment, the Montana

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[21] PPLM asserts that the concept of "seasonable attainment" referenced in Allegheny and Roosevelt requires the Department to either adjust-down (under-assess) PPLM's unregulated electric generation property or adjust-up (over-assess) regulated electric generation property in Montana in order to obtain "seasonable attainment" of all Class 13 electric generation property. As a threshold matter, this proposition is contrary to Montana's statutory requirement for 100% market value appraisals and the principle that equalization results when all properties within a statutory class are assessed at or near market value. Barron, 245 Mont. at 112, 799 P.2d at 540. Moreover, neither Allegheny nor Roosevelt found the failure to obtain "seasonable attainment" as an independent equal protection violation. The U.S. Supreme Court tangentially referred to "seasonable attainment" in the context of repudiating the assessor's argument that the subject periodic adjustment process was sufficient to obtain seasonable attainment of *similarly-situated* property and to thereby preclude discriminatory characterization of the acquisition value policy at issue. See Allegheny, 488 U.S. at 343-44, 109 S.Ct. at 637-38; accord Roosevelt, ¶ 45. Thus, the concept of "seasonable attainment" has no relevance unless there is unequal treatment of *similarly-situated* Class 13 electric generation property or unless a rational basis does not exist for unequal treatment of *similarly-situated* property. See Nordlinger v. Hahn (U.S. 1992), 505 U.S. 1, 16, 112 S.Ct. 2326, 2335 (Allegheny "was the rare case where the facts precluded any plausible inference that the reason for unequal assessment practice was to achieve the benefits of an acquisition value-tax scheme"); Fitzgerald v. Racing Assoc. of Central Iowa (U.S. 2003), 539 U.S. 103, 109-10, 123 S.Ct. 2156, 2160 (similarly distinguishing Allegheny).

Supreme Court held, as in Allegheny, that, as applied to Class 4 properties that had depreciated upon re-appraisal, the 2% phase-in provision was not rationally related to Montana's legitimate interest in limiting tax increases because it resulted in below-market assessment of appreciating properties and above-market assessment of depreciating properties. Roosevelt, ¶¶ 31-38.

In Barron, the Montana Supreme Court considered a statutory provision for assessment of residential properties based on a "stratified sales assessment ratio study" for each tax year. Barron, 245 Mont. at 102-04, 799 P.2d at 534-35. The Legislature's asserted purpose in enacting this provision was to "adjust current appraised values rather than to reappraise property" in order to "achieve equalization" across the state. Id. at 105, 799 P.2d at 536. However, the Montana Supreme Court found that the new assessment scheme discriminated between similar properties because it resulted in significant valuation increases for properties that were already appraised at or near their actual sales value in contrast to relatively insignificant increases for properties known to be already significantly under-appraised. Barron, 245 Mont. at 108, 799 P.2d at 538. Further finding that this discriminatory effect was not rationally related to the asserted state interest of adjusting residential property values to achieve equalization across the state, Id. at 108, 799 P.2d at 538, the Montana Supreme Court held that the discriminatory effect and

resulting disproportionate tax burden violated the equal protection safeguards of the U.S. and Montana constitutions. Barron, 245 Mont. at 111, 799 P.2d at 540.[22]

Unlike Allegheny, this case does not involve an acquisition-value assessment scheme or practice. Further, unlike in Allegheny, Roosevelt, and Barron, this case does not involve unequal treatment of *similarly-situated* properties. Although the PPLM, PSE, and Avista properties are similar insofar that they all constitute Class 13 electric generation property, they are nonetheless not similarly-situated within Class 13 in regard to market value due to the limiting effect of regulation on the market value of PSE, Avista, and other regulated utilities. Moreover, unlike in Allegheny, Roosevelt, and Barron, even if PPLM's unregulated property and the regulated PSE/Avista properties are characterized as similarly-situated for equal protection purposes, consideration of the effect of regulation on the market value of the regulated PSE and Avista properties rationally furthers Montana's legitimate interest under § 15-8-111, 15-7-112, and 15-1-101(1)(e), MCA, in valuing electric

[22] As in Allegheny and in reference to Larson v. State (1975), 166 Mont. 449, __, 534 P.2d 854, 857, the Montana Supreme Court also tangentially addressed the concept of "seasonable attainment," not as an independent equal protection violation, but rather, in the similar context of noting that the Department failed to show that the subject disparity was only temporary and would shortly be remedied by operation of existing law or policy. See Barron, 245 Mont. at 110-11, 799 P.2d at 539-40. Thus, like Allegheny and Roosevelt, the reference to "seasonable attainment" in Barron stands only for the proposition that, except for temporary valuation disparities, *similarly-situated* properties must be appraised at 100% of market value using a similar method of appraisal.

generation property at 100% of fair market value considering all relevant facts and circumstances. Thus, contrary to PPLM's assertion, Allegheny, Roosevelt, and Barron are all distinguishable here.

In summary, as adjusted by STAB for 2000-02, PPLM's unregulated electric generation property is valued at or near 100% of fair market value as required by §§ 15-8-111, 15-7-112, and 15-1-101(1)(e), MCA. Moreover, PPLM has not shown that the Department under-valued the still-regulated electric generation property of PSE, Avista, or other Montana generators for 2000-02. In the wake of deregulation of the electric power industry, unregulated electric generation property has significantly greater market value than regulated electric generation property due to its greater profit potential. Although STAB and the Department reasonably disagree about how to interpret the available valuation data for PPLM, Montana has used the same unit assessment methodology to appraise all Class 13 electric generation property in Montana. The significant disparity in valuation between the electric generation property of PPLM and PSE/Avista for 2000-02 results solely from the significant differences in market value of the otherwise similar properties in the respective legal and economic environments in which they respectively operate. Consequently, under the regulatory status quo for 2000-02, the otherwise similar electric generation properties of PPLM and

PSE/Avista are dissimilar in fact and as a matter of law for purposes of equal protection. Therefore, the disparate valuations for PPLM and PSE/Avista for 2000-02 do not constitute or result in classification or discrimination for purposes of constitutional equal protection.

To the extent that the disparate valuations for PPLM and PSE/Avista for 2000-02 arguably constitute or result in classification or discrimination based on regulatory status, Montana's valuations of Class 13 electric generation property based on consideration of relative regulatory status rationally furthers Montana's legitimate state interest under §§ 15-8-111, 15-7-112, and 15-1-101(1)(e), MCA, and Mont. Const. art. VIII, § 3, in valuating all taxable property at 100% of fair market value upon consideration of all relevant facts and circumstances. Consequently, whether the result of classification or discrimination on the basis of regulatory status or not, the significant property tax burden disparity between the unregulated PPLM electric generation property and the otherwise similar regulated property of PSE/Avista does not violate the equal protection guarantees of the Fourteenth Amendment of the U.S. Constitution and Mont. Const. art. II, § 4.

ORDER AND JUDGMENT

For the foregoing reasons, the Court hereby orders, adjudges,

and decrees as follows:

(1) STAB had jurisdiction to adjust the Department's appraised value of PPLM's property for tax years 2000-01;

(2) in regard to STAB's adjustments of the Department's 2000-02 valuations of PPLM's Class 13 electric generation property, STAB's findings of fact are not arbitrary or clearly erroneous, it did not abuse its discretion, and its conclusions of law are correct. Therefore, pursuant to §§ 15-2-301(5) and 2-4-704(2), MCA, the Court hereby affirms STAB's adjusted valuations of PPLM's Class 13 property for 2000-02[23];

(3) in regard to STAB's adjustments to the Department's 2000-02 valuations of PPLM's Class 5 pollution control equipment, STAB's findings of fact are not arbitrary or clearly erroneous, it did not abuse its discretion, and its conclusions of law are correct. Therefore, pursuant to §§ 15-2-301(5) and 2-4-704(2), MCA, the Court hereby affirms STAB's adjusted valuations of PPLM's Class 5 property for 2000-02[24]; and

(4) as applied to PPLM for tax years 2000-02 and as adjusted by STAB, the Montana's appraisal methodology and resulting assessments for 2000-02 did not unequally assess PPLM's Montana property in relation to other electric generation properties in Montana and did not result in a disparate tax burden in violation of the equal protection clauses of the Fourteenth Amendment of the U.S. Constitution and Mont. Const. art. II, § 4.

SO ORDERED this 28th day of April, 2006.

DIRK M. SANDEFUR
DISTRICT JUDGE

[23] See page 8, *infra*.
[24] See page 8, *infra*.

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DA 07-0356

IN THE SUPREME COURT OF THE STATE OF MONTANA

2008 MT 403

OMIMEX CANADA, LTD.,

Plaintiff and Appellant,

v.

STATE OF MONTANA, DEPARTMENT OF REVENUE,

Defendant and Appellee.

APPEAL FROM: District Court of the First Judicial District,
In and For the County of Lewis and Clark, Cause No. BDV-2004-288
Honorable Jeffrey M. Sherlock, Presiding Judge

COUNSEL OF RECORD:

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For Amicus Curiae:

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Submitted on Briefs: July 9, 2008

Decided: December 2, 2008

Filed:

Clerk

District Court Judge Robert L. Deschamps, III delivered the Opinion of the Court.

¶1 Omimex Canada, Ltd. ("Omimex") appeals from the judgment of the First Judicial District Court, Lewis and Clark County, declaring that the Montana Department of Revenue ("DOR") may centrally assess Omimex's property and classify it under § 15-6-141, MCA, as class nine property. We reverse.

¶2 Omimex raises several issues on appeal, which we consolidate and restate as follows:

¶3 Did the District Court err in considering Omimex's operating characteristics in concluding Omimex was "operating a single and continuous property operated in more than one county or more than one state" and is, therefore, subject to central assessment pursuant to § 15-23-101, MCA?

¶4 Did the District Court err in concluding all of Omimex's property should be centrally assessed pursuant to § 15-23-101, MCA, and classified as class nine property pursuant to § 15-6-141, MCA?

¶5 Did the District Court err in concluding Omimex did not meet its burden of proof for its equalization and equal protection challenges?

BACKGROUND

¶6 The facts of the case are largely undisputed. Omimex, a subsidiary of an international oil and gas corporation, owns an interest in five distinct large and scattered smaller properties in Montana. Omimex extracts primarily natural gas from these properties. The properties are not physically connected by Omimex-owned facilities, are not dependent on one another, and may be operated independently. Nonetheless, most of

the gas produced at these facilities is sold to a single buyer. The properties are supervised by a Montana-based foreman and are centrally managed out of Omimex's Texas headquarters.

¶7 The five main Omimex Montana properties are known as the Cut Bank Area properties ("Cut Bank properties"), the Shelby Area properties ("Shelby properties"), the Bowdoin properties, the Regan properties and the Battle Creek properties. These properties cover some 2.2 million acres containing approximately 1,450 wells. The wells collectively produce over 10 million cubic feet of natural gas a day and slightly less than 600 barrels of oil a day. Each property has gathering lines that, at low pressure, move untreated gas or oil from Omimex's and often other parties' individual wells to central collecting points for further transmission in large high pressure lines.

¶8 The collection point for the Cut Bank properties includes an Omimex plant where gas is treated to remove impurities and by-products before the gas is moved on in a large high-pressure line to a junction with another entity's transmission pipeline. Some of the properties cover more than one county (Cut Bank and Shelby properties), and at least one (Bowdoin properties) crosses the international border into Canada. The Regan properties produce only oil, which is sold to a ground transporter. While Omimex produces and sells some oil and other petroleum products, its main focus in Montana is natural gas. The parties and the District Court consistently considered it to be a natural gas company.

¶9 Most Omimex gas is sold to an entity known as WPS Energy Services, Inc. ("WPS"). Ownership of the gas is transferred to WPS at various locations where there are junctions between Omimex pipelines and transmission pipelines owned by third party

entities. In at least three of the properties (Shelby, Bowdoin, and Battle Creek) Omimex owns and operates high pressure transmission lines that carry accumulated gas owned by Omimex. For a fee, other entities may utilize the Omimex lines to convey their product to junctions with pipelines owned by third parties. At these junctions, the ownership of Omimex gas is transferred to WPS or another buyer, all of whom then transport the gas to distant markets. Omimex has a permit to import and export gas and owns a right to transport gas on some of the third party pipelines but not all of them. WPS transports the Omimex gas it purchases in cross-Canadian pipelines owned by other entities. WPS eventually distributes and sells the gas to consumers in other parts of North America.

¶10 Four of the five Omimex Montana properties (Cut Bank, Shelby, Bowdoin, and Regan properties) were at one time owned and operated by the former Montana Power Company ("MPC") or one of its subsidiaries. Two of the former MPC properties, the Cut Bank and Shelby properties, were a part of the integrated natural gas production and distribution ("wellhead to burner tip") system operated by the MPC until the mid-1990s prior to that company's deregulation and ultimate piecemeal divestiture of its assets.

¶11 In Montana, property is assessed for taxation by DOR. Most property is assessed county by county by DOR personnel. This is called "local assessment." Exceptions include the statewide or "central" assessment of property owned in multiple counties or states by certain owners as defined by statute. Section 15-23-101, MCA, provides, "[t]he department shall centrally assess each year . . . (2) property owned by a corporation or other person operating a single and continuous property operated in more than one county or more than one state, including, but not limited to . . . natural gas or oil pipelines . . . ."

¶12 The Cut Bank, Shelby and, apparently, the Regan properties were centrally assessed by the DOR when these properties were owned and operated by the MPC. The Bowdoin properties, while owned by a MPC subsidiary, were locally assessed because the gas from this property was sold differently than the rest of MPC's gas. The Battle Creek properties were not a part of the MPC system and were previously assessed locally.

¶13 After deregulation in 1997, the MPC properties were transferred by MPC to a subsidiary named Entech. In 2000, Entech sold these properties and others to PanCanadian Energy Resources, Inc., later called EnCana. Along the way EnCana also acquired the Battle Creek properties. In 2003, Omimex purchased the properties involved in this case from EnCana, while other former MPC properties owned by EnCana were sold to other buyers.

¶14 The DOR has been centrally assessing the Omimex properties because some properties cross county lines and because all are operated by Omimex as a functional single entity or "unity of operation." Omimex does not contest DOR's valuation but has advanced several arguments in support of its contention that the properties should be assessed locally, not centrally. Because Omimex's properties are centrally assessed, DOR has classified the property as class nine property under § 15-6-141, MCA, which is taxed at a rate of 12%. Omimex contends that its properties should be locally assessed and classified as class eight properties under § 15-6-138, MCA, which are taxed at a rate of 3%.

¶15 The District Court agreed with the DOR and upheld the central assessment and class nine classification. Omimex appeals.

STANDARD OF REVIEW

¶16 The standard of review for issues of law is de novo. *Citibank (South Dakota) N.A. v. Dahlquist,* 2007 MT 42, ¶ 8, 336 Mont. 100, ¶ 8, 152 P.3d 693, ¶ 8. The standard of review of any disputed issues of fact is clearly erroneous. *Leichtfuss v. Dabney,* 2005 MT 271, ¶ 20, 329 Mont. 129, ¶ 20, 122 P.3d 1220, ¶ 20.

DISCUSSION

¶17 Omimex does not dispute the DOR's valuation of its property. The fundamental question in this case is whether Omimex's property should be taxed at a rate of 12% under § 15-6-141, MCA, or at a rate of 3% under § 15-6-138, MCA.

¶18 Regardless of whether Omimex's property is centrally or locally assessed, its tax rate class is determined by the application of the physical attributes of Omimex's Montana properties to the terms of the property classification statutes, §§ 15-6-138 and -141, MCA.

¶19 Pursuant to § 15-6-138, MCA,

> (1) Class eight property includes:
>
> . . .
>
> (c) all oil and gas production machinery, fixtures, equipment, including pumping units, oil field storage tanks, water storage tanks, water disposal injection pumps, gas compressor and dehydrator units, communication towers, gas metering shacks, treaters, gas separators, water flood units, gas boosters, and similar equipment that is skidable, portable, or movable, tools that are not exempt under 15-6-219, and supplies except those included in class five;

. . .

(n) all other property that is not included in any other class in this part, except that property that is subject to a fee in lieu of a property tax.

. . .

(4) Class eight property is taxed at 3% of its market value.

¶20 Pursuant to § 15-6-141, MCA,

(1) Class nine property includes:

. . .

(b) allocations for centrally assessed natural gas companies having a major distribution system in this state; and
(c) centrally assessed companies' allocations except:
(i) electrical generation facilities classified under 15-6-156;
(ii) all property classified under 15-6-157;
(iii) all property classified under 15-6-158 and 15-6-159;

. . .

(2) Class nine property is taxed at 12% of market value.

¶21 The applicable rules of statutory construction to be used to construe these statutes are straightforward. When construing statutes, the court "is simply to ascertain and declare what is in terms or in substance contained therein . ... ." Section 1-2-101, MCA. The specific must prevail over the general. Section 1-2-102, MCA. Related to this is the canon of statutory construction known as *expressio unius est exclusio alterius* (the expression of one thing [in a statute] implies the exclusion of another). S*ee e.g. Dukes v. City of Missoula,* 2005 MT 196, ¶ 15, 328 Mont. 155, ¶ 15, 119 P.3d 61, ¶ 15 (applying the canon to enforcement of the Montana Scaffold Act); *Harris v. Smartt,* 2003 MT 135,

¶ 17, 316 Mont. 130, ¶ 17, 68 P.3d 889, ¶ 17 (applying the canon to the Montana Constitution); *Mitchell v. University of Montana*, 240 Mont. 261, 265, 783 P.2d 1337, 1339 (1989) (applying the canon to the statutory definition of "local government units"). If the intent of the legislature can be determined from the plain meaning of the words used in the statute, the plain meaning controls and the Court need go no further. *Western Energy Co. v. State, Dept. of Rev.*, 1999 MT 289 ¶ 11, 297 Mont. 55, ¶ 11, 990 P.2d 767, ¶ 11. Finally, tax statutes are to be strictly construed against the taxing authority and in favor of the taxpayer. *Western Energy*, ¶ 10.

¶22 Prior to 1999, § 15-6-141, MCA, contained not only the provisions of subsection (1)(b) regarding centrally assessed natural gas companies with major distribution systems, but also contained a separate provision under the exception provisions of subsection (1)(c). This provision was former § 15-6-141(1)(c)(i), MCA, until it was amended by Chapter 556, 1999 Session Laws. Before the amendment, the pertinent parts of the statute read: "(1) Class nine property includes . . . (b) allocations for centrally assessed natural gas companies having a major distribution system in this state; and (c) centrally assessed companies' allocations except: (i) electric power and natural gas companies' property . . . ." The 1999 amendments to (1)(c)(i) substituted "electrical generation facility property included in class thirteen" for "electric power and natural gas companies' property." Subsequent amendments modified the provision into its current form.

¶23 The Montana Legislature's intent in enacting the "Electrical Generation Tax Reform Act," Section 1, Chapter 556, 1999 Montana Session Laws, was to reform

taxation of electrical generation facilities in the aftermath of the restructuring of the electric utility industry following its 1997 deregulation. The natural gas industry is not mentioned anywhere within Chapter 556, 1999 Montana Session Laws. From this we conclude that the 1999 amendments to § 15-6-141, MCA, were not intended to alter the status quo regarding natural gas companies' tax classification.

¶24 Under the statute as it existed prior to the 1999 amendment, it was clear that the legislature intended to exempt centrally assessed natural gas companies from class nine *unless* the companies had a major distribution system in the state. Absent any statement of legislative intent to the contrary, this remains the rule.

¶25 Tax statutes must be construed in favor of the taxpayer. The explicit inclusion of "centrally assessed natural gas companies having a major distribution system in this state" implies the exclusion of all other centrally assessed natural gas companies under the *expressio unius est exclusio alterius* canon. The specific description of "centrally assessed natural gas companies having a major distribution system in this state" in § 15-6-141(1)(b), MCA, prevails over the general catch-all provision for "centrally assessed companies" in § 15-6-141(1)(c), MCA. If the legislature had intended to place all centrally assessed natural gas companies into class nine, it had two simple ways to do so: it could have deleted § 15-6-141(1)(b), MCA, altogether or, if for some reason the legislature wanted to single out centrally assessed natural gas companies to be certain they would all be placed in class nine, it could have deleted the qualifier "having a major distribution system in this state." It did not do either.

¶26 Assuming, arguendo, that the District Court was correct in upholding DOR's central assessment of Omimex, and that Omimex is properly a "centrally-assessed natural gas company," it still does not have a major distribution system in this state as required by § 15-6-141(1)(b), MCA. Omimex's properties are manifestly designed not to distribute, but rather to accumulate natural gas from hundreds of individual wells to central points where the gas is commingled and delivered to a single buyer. It is the buyer who then transports the gas to distant locations where it is finally distributed to consumers. Therefore, Omimex's properties, regardless of whether they are centrally or locally assessed, should be classified as § 15-6-138(1)(c) or (n), MCA, class eight property subject to a 3% tax rate.

¶27 For the foregoing reasons it is not necessary to address whether the District Court was in error when it upheld the central assessment of Omimex's property since where the property is assessed does not make any difference for its classification. Similarly, since we hold that the District Court did err in upholding the DOR class nine classification, it is not necessary to address Omimex's due process and equal protection arguments concerning that classification. Because the District Court erred in determining that the properties should be classified as class nine properties under § 15-6-141, MCA, we reverse and remand for entry of an amended judgment classifying the Omimex properties as class eight properties under § 15-6-138, MCA.

/S/ ROBERT L. DESCHAMPS, III
District Court Judge Robert L. Deschamps, III
sitting for Justice Brian Morris

We concur:

/S/ KARLA M. GRAY
/S/ PATRICIA COTTER
/S/ JOHN WARNER
/S/ W. WILLIAM LEAPHART
/S/ JIM RICE

/S/ JOE L. HEGEL
District Court Judge Joe L. Hegel
sitting for Justice James C. Nelson

MONTANA FIRST JUDICIAL DISTRICT COURT
LEWIS AND CLARK COUNTY

OMIMEX CANADA, LTD., Plaintiff, v. STATE OF MONTANA, DEPARTMENT OF REVENUE, Defendant.	Cause No. BDV-2004-288 **FINDINGS OF FACT, CONCLUSIONS OF LAW AND ORDER**

This matter was heard on September 18, 19 and 20, 2006, before the Court sitting without a jury. Omimex Canada, LTD (hereinafter Omimex) was represented by James P. Sites and Jared M. Le Fevre, of the law firm Crowley, Haughey, Hanson, Toole & Dietrich, P.L.L.P.. The State of Montana, Department of Revenue (hereinafter DOR) was represented by Charlena Toro and David L. Ohler. Both parties presented witnesses and evidence. From the evidence presented, the Court enters the following:

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FINDINGS OF FACT

According to the Pre-Trial Order, the parties have agreed that the following facts are admitted and agreed to be true.

1. This is a complaint for declaratory judgment [pursuant to Section 15-1-406, MCA] by [Omimex], a Delaware corporation authorized to do business in Montana.

2. Omimex's Montana properties generally consist of the following:

Cut Bank Area Properties
- Cut Bank Gathering
- Cut Bank Gas Plant
- Big Rock Gathering
- Cut Bank Pipeline

Shelby Area Properties
- Kevin Sunburst Gathering
- East Keith Gathering
- Utopia Gathering
- East Keith Pipeline

Bowdoin Properties
- Bowdoin Field Gathering
- Whitewater Pipeline

Regan Properties
- Regan Field Gathering

Battle Creek Properties
- Battle Creek Gathering
- Chinook Pipeline

3. These assets were purchased by Omimex from EnCana Energy Resources, Inc. (hereinafter EnCana), in 2003.

4. From the above properties, Omimex sells crude oil, butane, propane, natural gasoline, and natural gas.

5. The above properties consist of hundreds of miles of natural gas and oil pipelines and approximately 1,400 wells.

6. Omimex's corporate headquarters is in Forth Worth, Texas.

7. The president and owner of Omimex, Naresh Vashisht, makes all key management decisions out of the corporate headquarters.

8. The field operations of Omimex's Montana properties are managed by its production foreman, Paul DeKaye, located in Cut Bank, Montana.

9. Omimex moves in its pipelines gas that it owns (equity gas), gas in which Omimex does not have an interest (third-party gas), and gas in which Omimex owns a working interest along with other

owners.

10. The Cut Bank pipeline, owned and operated by Omimex, crosses the county line between Glacier and Toole Counties.

11. The East Keith pipeline, owned and operated by Omimex, runs from Hill County through Liberty County into Toole County.

12. Omimex has a gas marketing agreement with Wisconsin Public Services (hereinafter WPS).

13. Omimex does not dispute the valuation of $16,598,716 assigned to its properties by the Department of Revenue.

(Pre-Trial Order, at 1-3.)

As noted above, the parties agree with the valuation placed on Omimex's properties by the DOR. However, the parties dispute whether the assessment of the properties should be done by local assessment or central assessment. The DOR argues that the property in question should be centrally assessed pursuant to Section 15-23-101, MCA. Thereafter, having made such an assessment, the DOR feels that the taxation of the properties should be pursuant to Section 15-6-141, MCA, which provides for a 12 percent tax rate. Omimex, on the other hand, seeks a declaration that the taxation of its property for tax year 2004 be accomplished pursuant to Section 15-6-138, MCA, which provides that class eight property be taxed at 3 percent of its market value.

Omimex is a subsidiary of Omimex Resources, Inc. In addition to Omimex Canada, Omimex Resources has three other subsidiary companies: Omimex Energy, Inc., Omimex International Corporation and Omimex DeColumbia. Omimex Resources and its subsidiaries operate in Michigan, Texas, Oklahoma, North Dakota, New Mexico, Columbia, Canada, and Montana.

Omimex Canada is engaged in the natural gas and oil business in

Montana and Canada. Omimex has a significant leasehold interest in Montana. Omimex owns an interest in approximately 1,450 wells in Montana, and its leases cover 2.2 million acres. Omimex's properties produce over 10 million cubic feet of natural gas a day, and a little less than 600 barrels of oil a day. Omimex's properties include pipelines, well equipment, compressors, gas processing plants, office buildings, and field offices.

In order to move natural gas from where it is located in the ground to retail markets, where it is utilized, the natural gas system includes several discrete operations or processes. Those include exploration for and production of natural gas, gas gathering, gas processing, gas transmission, and gas distribution. Some natural gas companies engage almost entirely in one of those areas, such as distribution or exploration or production. Other companies occupy a wider niche in the vertical chain of the natural gas industry. Omimex engages in exploration and production of natural gas, the gathering of natural gas for itself and third parties, the processing of natural gas for itself and for third parties, and the transportation of natural gas for itself and third parties. Omimex claims that is only an exploration and production company.

The Omimex properties include various natural gas fields located in northern Montana. Below, the Court will set forth the general nature of these areas. Generally, it is accepted as true by the parties that the various pipelines are not connected together with any property owned by Omimex.

Cut Bank Area Properties

The Cut Bank gas gathering system includes some 225 miles of gathering pipeline. These gas gathering pipelines are located in both Glacier and Toole Counties, and some of the pipelines cross the line between Glacier and Toole Counties. Also included in the Cut Bank area is the Cut Bank processing plant. This plant treats

natural gas so that is can be "transmission quality gas." The plant not only processes natural gas owned by Omimex, but also gas owned by third parties. The Cut Bank processing plant creates between 5,000 and 6,000 gallons of propane daily, between 5,000 and 6,500 gallons of butane daily, and between 4,000 and 5000 gallons daily of natural gasoline. These by-products from the processing of Omimex's and third-parties' gas, are sold by Omimex on behalf of itself and on behalf of the third-parties who own the gas Omimex processes at the plant.

The Cut Bank gathering pipeline, on a daily basis, moves approximately 4,400 MMBTU of Omimex gas and approximately 2,900 MMBTU of third-party gas.

The Cut Bank properties also includes what is known as the Big Rock gathering area. This includes approximately 52 miles of gathering pipeline. This gathering pipeline moves not only 20,000 MMBTU of Omimex's gas on a daily basis, but also 17,000 MMBTU of third-party gas. This area also includes what is known as the Regan 4-inch cross-border gas pipeline. This pipeline crosses the border between Glacier County, Montana, and Canada. It brings natural gas to Montana and is regulated by the Canadian Natural Energy Board. The Regan pipeline also carries third-party gas for a fee.

Shelby Area Properties

The Shelby area properties include what is known as the Kevin Sunburst gathering field, which includes approximately 43 miles of gathering pipeline, along with associated equipment. The Kevin Sunburst gathering field moves some third-party gas for a fee.

The Shelby area properties also include the East Keith gathering system which has approximately 125 miles of gathering pipeline. This area also includes the 35-mile long East Keith pipeline which crosses Hill, Liberty and Toole Counties and

moves, on a daily basis, 1,700 MMBTU of Omimex's gas and 1,100 MMBTU of third-party gas.

The Shelby area properties also include what is known as the Utopia gathering field, which includes approximately 5 miles of gathering pipeline that also moves Omimex gas, along with third-party gas.

Bowdoin Properties

The Bowdoin properties include the Whitewater natural gas transmission line, which will be mentioned in more detail later.

The Bowdoin system also includes a gathering pipeline that crosses the Canadian-U.S. border. Unlike the other properties mentioned herein, the Bowdoin property at one time was owned by an entity named NARCO. NARCO was a subsidiary of the Montana Power Company (MPC). For purposes here, the important point is that the NARCO properties were, at one time, locally assessed. Although owned by a subsidiary of MPC, the property was not part of the regulated utility supervised by the Montana Public Service Commission. In the past, the NARCO gas was sold in a different manner than the rest of MPC's gas.

The Bowdoin properties were purchased by Omimex at the same time as the other properties mentioned in this document.

Regan Property

The Regan property is an oil field located in Glacier County. It includes some oil wells and storage tanks. The oil produced from these wells and tanks is sold by Omimex to Cenex.

Battle Creek Properties

The Battle Creek properties include approximately 40 miles of gathering pipeline from what is known as the Xeno gas field. This area also includes the

Chinook natural gas transmission line that goes to the U.S.-Canadian border. It is important to note here that the Battle Creek properties were, at one time, locally assessed when owned by an entity named Xeno. This property was not owned by MPC.

The Court has earlier referenced certain transmission lines. The parties have debated the difference between transmission lines and gathering lines. Gathering lines are generally low pressure lines that collect natural gas. The lines are in a spider web formation and are of varying sizes and produce gases of varying quality. The gas is usually not under pressure and is untreated. Transmission lines, on the other hand, generally operate under high pressure and are of a higher quality material, such as steel. They generally move gas that has been treated to remove contaminants. That gas is referred to as transmission quality gas. Generally, transmission lines are noted for moving third-party gas for a fee.

The Court considers at least three of Omimex's pipelines to be transmission lines - the East Keith pipeline, the Chinook pipeline and the Whitewater pipeline. In this regard, the Court has had reference to Exhibit 10, which is a purchase and sale agreement whereby EnCana sold the subject properties to Omimex. Exhibit B-2 to that document, contained at Bates-stamp page 0000616, contains a list of the properties sold. The Whitewater pipeline is referred to as a "DOT transmission line." Further, that document refers to the Chinook pipeline as a "transmission line." The East Keith pipeline crosses between Hill, Liberty and Toole Counties in northern Montana. It is approximately 35 miles long and carries approximately 1,700 MMBTU of Omimex gas, along with 1,100 MMBTU of third-party gas. This gas is transferred to NorthWestern Energy at the Telstead Junction, where the East Keith pipeline meets the NorthWestern Energy transmission line.

The Chinook pipeline carries natural gas from the Battle Creek area. This pipeline is six inches in diameter and is 16 miles long. It is located entirely in Blaine County. The Chinook pipeline operates under 900 to 1,100 pounds of pressure and moves, on a daily basis, 2,800 MMBTU of Omimex's gas, along with 21,000 MMBTU of third-party gas. Omimex charges third parties a fee to move their gas and to compress that gas prior to being placed in this pipeline. The Chinook pipeline takes the Battle Creek gas to the Canadian border. There, the Many Islands pipeline takes the gas to the Trans-Canadian pipeline, where Omimex's gas is sold to WPS. Because Omimex imports and exports gas over the Canadian border, Omimex must file with the Federal Energy Regulatory Commission (FERC) information concerning the Chinook pipeline.

The Whitewater pipeline moves Omimex and third-party gas in Phillips County. This gas is transferred to the Northern Border pipeline at the Canadian border, where it is sold to WPS. This pipeline is 19 miles long, is 12 inches in diameter and is under 1,000 pounds of pressure. Again, the Whitewater pipeline transports third-party gas for a fee, moving approximately 3,300 MMBTU daily of Omimex gas and approximately 22,300 MMBTU of third-party gas.

Omimex sells all of its natural gas to an entity known as WPS Energy Services, Inc. (Ex. 67.) Generally speaking, the gas that is sold to WPS is done so at five points. These points are generally the same as where MPC sold its natural gas. Although Omimex sells its gas to WPS, the transmission pipelines on which WPS moves the gas are not owned by WPS.

The Omimex gas is put into the NorthWestern Energy system at Telstead, Utiopia and Cut Bank. Omimex does not have a contract with NorthWestern Energy and has no individual right to use the NorthWestern Energy transmission lines.

The interconnection agreement involved is between WPS and NorthWestern Energy.

Omimex gas is also transferred from the Whitewater pipeline, which takes the Bowdoin gas to the Northern Border pipeline. At that interconnection, WPS again takes possession of the gas and moves it along the Northern Border pipeline. Likewise, as mentioned earlier, the Chinook pipeline carries gas north to the Canadian border, where it is transported on the Many Islands pipeline to the Trans-Canadian pipeline where, again, WPS takes title to the gas and moves it east to its eventual marketing area.

In addition to the pipeline properties mentioned above, Omimex owns other property of value in Montana. Omimex has a governmental permit to import and export large quantities of natural gas to and from Canada any where along the Canadian border. It also has permission at the Chinook crossing to import and export gas. Omimex also has a right to transport natural gas on the Northern Border pipeline and the Many Islands pipeline. (Storms Test., at 329-30, 298-99.) Omimex also owns numerous easements and lease holds to generate natural gas and to operate its various pipelines. Thus, it appears that Omimex is more than an exploration and production company, since it not only produces natural gas and explores for it, but it transports its own and others' natural gas, processes natural gas, imports and exports natural gas at the Canadian border, and markets natural gas and by-products for itself and others.

All of Omimex's properties involved here, with the exceptions earlier noted, were at one time owned and operated by MPC. Also, except as earlier noted, all of the properties have been centrally assessed in the past and operated as an integrated business unit owned by various other companies. Most of the properties were owned by MPC, which was regulated by the Montana Public Service Commission as a utility. MPC transferred the properties to its subsidiary Entech. In 2000, Entech sold the

property to PanCanadian Energy Resources, Inc., which eventually became EnCana. All of the property mentioned in this document, whether previously owned by MPC or not, was transferred by EnCana to Omimex in October 2003. (Ex. 10.) EnCana had tried to sell the property as individual parcels but was unable to do so, and all of the Omimex properties were purchased as one parcel from EnCana. Omimex, however, did not buy all of EnCana's property, as other EnCana property was sold to other individuals.

As earlier noted, Omimex's natural gas operations generally connect to the larger transmission lines mentioned above in the same places as did MPC's. It is undisputed that the various gathering areas owned by Omimex are not physically connected to each other with Omimex owned property.

It is also undisputed that Omimex is not regulated and does not operate as a public utility system. One hundred percent of Omimex's gas is sold to WPS under a single sales agreement. WPS has interconnection agreements with NorthWestern Energy. The sale of Omimex's gas to WPS occurs on the "input side" of compressors where the Omimex gas enters the large transmission lines mentioned above.

It is also undisputed that Omimex's various gas fields are not specifically dependent on each other. For example, if a gathering pipeline in the Cut Bank area ceases to operate, that would have no effect on the Bowdoin, Battle Creek or other gathering systems mentioned here. It further appears that the gas produced between the various fields is of varying quality and that the wells are of differing depths and types.

Although Omimex's properties are spread over a large area, they are all ultimately managed out of Fort Worth, Texas, where Omimex is headquartered. All accounting for the various properties mentioned in this document is done at the Fort

Worth headquarters. Further, all engineering decisions are made in Fort Worth, and Fort Worth provides centralized management and key decision-making for the Omimex properties in Montana.

The Court has also seen Exhibit 5, which is a December 9, 2002, document prepared by the DOR entitled "Central Assessment Position Paper." That document indicates that gathering lines owned by a centrally assessed company are considered operating property of the centrally assessed company. The criteria for central assessment require that the property be one specifically listed in Section 15-23-101(1)-(3), MCA. The document also requires that the areas be physically connected or crossing county or state boundaries. In lieu of physical connection, the document indicates that a unity of operation can be substituted for a physical connection. This requires that the property be functionally operated as single entity, even though it does not have physical connection.

Testifying at the hearing was DOR witness Gene Walborn. Walborn indicated that, in addition to Exhibit 5, the DOR has unwritten policy guidelines in determining whether gas lines are to be centrally or locally assessed. If strictly gathering lines, the lines are to be locally assessed even if they cross county lines. If, however, the line is a transmission line, it is to be centrally assessed if it crosses a county line. Further, Walborn indicated that Omimex not only has a transmission line crossing county lines (East Keith pipeline), but it also operates all of its properties in a continuous and unitary fashion.

If a centrally assessed taxpayer, according to Walborn, has non-operating property, the non-operating property is to be locally assessed. For example, PPL Montana may own vacant land that is not operating to help PPL to produce energy. Walborn further indicated that according to department policy, the property does not

need to be physically connected to be centrally assessed.

Each party produced expert witnesses. Omimex produced Dr. John Davis, who concentrates on unitary tax matters. He deals extensively in finance, economics and appraisal. According to Dr. Davis, Omimex's property is not a single and continuous operation as mentioned in Section 15-23-101, MCA. Dr. Davis noted the theory underlying central assessment of property: part of the value of an on-going operation may be lost if property is only assessed by local assessors. Dr. Davis indicated that centrally assessed property did not need to be physically connected. He noted that large manufacturing plants, railcar companies and airlines are not physically connected, yet they are centrally assessed. According to Dr. Davis, there is a value to the operating entity as a whole that would not be recognized if the properties were only assessed by local assessment. Dr. Davis testified that Omimex's properties are primarily gas gathering lines. The gas gathering lines are of all sizes and composition and operate under no pressure. If one field fails, the other fields will operate properly. According to Dr. Davis, gas gathering lines are not to be centrally assessed and are always locally assessed. Gas gathering lines, according to Dr. Davis, are distinguished by their differing qualities of gas from well-to-well and field-to-field. Further, gas gathering lines are usually not connected together, as is the case here, with other property owned by the taxpayer. Dr. Davis felt it significant that these properties are not interconnected by other properties owned by Omimex. If the lines were transmission lines, then, according to Dr. Davis, they would be appropriately centrally assessed. Generally, according to Dr. Davis, transmission lines usually have a rate base, are FERC regulated and allow a specific rate of return. Transmission lines generally constitute a singe line of a constant diameter, are usually made of steel, and operating under pressure. These transmission lines, according to Dr. Davis, usually

cross state lines.

The DOR, on the other hand, produced George Donkin, who has a master's degree in economics. Donkin concentrates in energy economics and has been familiar with these particular gas pipelines and fields from when they were owned by MPC. Donkin's report was received into evidence as Exhibit 75. Donkin felt that the Omimex properties were operating as a single and continuous property, properly centrally assessed. Donkin particularly noted that the properties have been centrally assessed in the past. Further, he noted that all the properties were sold as a unit, and that EnCana was unable to sell them as separate fields. This indicates to Donkin that the properties have an enhanced value when operated as an integrated business unit. Donkin also felt that the properties were properly centrally assessed since they met the statutory definition of property to be centrally assessed in the past. Donkin also relied on the PPL case, which will be dealt with by the Court in more detail later. Donkin noted that the statute, Section 15-23-101, MCA, requires central assessment if the property is a single and continuous property operated in more than one county. Donkin also noted that the fields do not operate as independent units. In this regard, he noted that there is one single gas marketing agreement between Omimex and WPS. That agreement has no reference to the individual pipelines or gas fields. All of Omimex's gas is managed as a unit and not pursuant to separate gas marketing agreements. Donkin also pointed to the centralized engineering and accounting functions that are performed in a centralized fashion out of Omimex headquarters in Fort Worth. Key management decisions are made in Fort Worth, and the company has but a single personnel policy and a health and safety policy that apply to all of its Montana and other employees. Donkin also felt that the Omimex system is similar to other centrally assessed pipeline properties, including Montana-Dakota Utilities, the

Havre Pipeline Company and NorthWestern Energy. These companies are operated as integrated units and move third-party gas for a fee.

Donkin also noted that the Omimex system is different from other pipeline companies that are not centrally assessed, even if those companies should have pipelines that cross county lines. Most important to Donkin's opinion is that, in his view, Omimex has ready access to the NorthWestern and other transmission lines due to its agreement with WPS. Donkin explained that FERC Order No. 636 required interstate natural gas transmission lines to provide services in a non-discriminatory fashion. The large transmission lines, such as NorthWestern Energy's, have to carry the natural gas owned by other parties. The FERC order had the effect of putting the pipeline companies out of the business of selling natural gas and, according to Donkin, now most of them move gas that is owned by third parties. According to Donkin, FERC Order No. 636 forbids the interstate gas pipeline companies from unreasonably denying transportation of third-party gas. According to Donkin, this rule and the interconnection agreement that WPS has with NorthWestern Energy allows Omimex to use these interstate transmission lines as its own. According to Donkin, the WPS interconnection agreement with the major transmission lines functionally operates as the interconnection agreement in the PPL case, which will be mentioned later. According to Donkin, Omimex does not need a gas transportation contract, since WPS has one. Since WPS has an interconnection agreement, the Omimex-WPS sales agreement functionally operates to allow Omimex the use of the NorthWestern Energy pipelines.

The Court became aware that certain pipeline companies are not centrally assessed but are locally assessed. These companies include Ocean Energy (now known as Devon), Encore Operating and Klabzuba. According to the DOR,

these companies have gathering lines and are to be locally assessed. There was some dispute as to whether any of these companies actually have gathering lines across county lines, but DOR witness Walborn indicated that even if some of the gathering lines might cross county lines, they would still be locally assessed. Further, some of the Ocean Energy lines were centrally assessed when that property was, at one time, owned by MPC. The Ocean Energy properties are now, as mentioned above, locally assessed.

From the foregoing Findings of Fact, the Court enters the following:

CONCLUSIONS OF LAW

This Court has jurisdiction of this case.

The Court must be mindful of the rules of interpretation to be used in cases such as this. Omimex has the burden of proving the DOR's decision incorrect. *See* Farmers Union Cent. Exch. v. Dep't of Revenue, 272 Mont. 471, 901 P.2d 561 (1995). In addition, if a statute can be construed in two ways, any doubt is to be resolved in favor of the taxpayer. Tax statutes are to be strictly construed against the taxing authority and in favor of the tax payer. W. Energy Co. v. Dep't of Revenue, 1999 MT 289, 297 Mont. 55, 999 P.2d 767. When interpreting a statute, the Court is to give great deference to the interpretation given by the agency charged with its administration. Dep't of Revenue v. Puget Sound Power & Light Co., 179 Mont. 255, 587 P.2d 1282 (1979).

The Court will first deal with Omimex's claim that the DOR has failed to equalize Omimex's property with others similarly situated, thus violating Article VIII, section 3, of the Montana Constitution and by denying Omimex equal protection. Article VIII, section 3, of the Montana Constitution requires that the State shall equalize the valuation of all property which is to be taxed in Montana. Also, the

Montana and United States Constitutions require that no party be denied equal protection in that similarly situated parties are to be treated the same.

The problem with Omimex's claim in this regard is that, although there has been some evidence concerning companies that are locally assessed (Ocean Energy and others), there is no particular evidence as to the nature of those companies' operations which would show the Court that the property of these other companies is similar to the properties here being operated by Omimex. Omimex operates in eight counties and Canada, moves a large amount of third-party natural gas, processes gas, and imports and exports gas from the United States and Canada. Omimex also operates at least three transmission pipelines, at least one of which crosses county lines.

The theory of equalization was addressed by the Montana Supreme Court in Dep't of Revenue v. State Tax Appeal Bd., 188 Mont. 244, 613 P.2d 691 (1980). In order for Omimex to prevail, the evidence presented must not be conjectural or speculative. Further, the burden is on the taxpayer to remove this determination from the realm of conjecture or speculation. Id., at 250, 613 P.2d at 694. Further, the taxpayer must show several elements, including that there are other properties within a reasonable area similar and comparable to his, the amount of assessment on these other properties, and the actual value of the comparable properties. Id. Here, Omimex has failed to show the similarity of the other properties to Omimex's properties, the amount of the assessments on these other properties, and the actual value of those comparable properties.

In addressing an equal protection claim, the first thing a court must do is identify the two classes and determine whether they are similarly situated. Matter of S.L.M., 287 Mont. 23, 32, 951 P.2d 1365, 1371 (1997). Here, there is no showing that

Omimex is similar to any other particular pipeline company.

Thus, the Court concludes that Omimex's challenge under Article VIII, section 3, of the Montana Constitution, along with the Montana Constitution's equal protection guarantees have not been proven and must fail.

The central question in this case is whether the Omimex properties were properly centrally assessed pursuant to Section 15-23-101, MCA, which provides:

> **Properties centrally assessed.** The department shall centrally assess each year:
> (1) the railroad transportation property of railroads and railroad car companies operating in more than one county in the state or more than one state;
> (2) property owned by a corporation or other person operating a single and continuous property operated in more than one county or more than one state, including but not limited to telegraph, telephone, microwave, and electric power or transmission lines; natural gas or oil pipelines; canals, ditches, flumes, or like properties and including, if congress passes legislation that allows the state to tax property owned by an agency created by congress to transmit or distribute electrical energy, property constructed, owned, or operated by a public agency created by congress to transmit or distribute electrical energy produced at privately owned generating facilities, not including rural electric cooperatives;
> (3) all property of scheduled airlines;
> (4) the net proceeds of mines, except bentonite mines;
> (5) the gross proceeds of coal mines; and
> (6) property described in subsections (1) and (2) that is subject to the provisions of Title 15, chapter 24, part 12.

The Court concludes that the Omimex properties were properly centrally assessed under Section 15-23-101, MCA. It appears clear that the Omimex properties are operated as a single and continuous property. The Court bases this conclusion on the testimony of George Donkin, who noted that all Omimex property mentioned herein is centrally managed out of Fort Worth, Texas, and that all Omimex gas is sold pursuant to one sales agreement. Further, the Omimex properties are located in more than one county. If property is operated as a single and continuous property in more than one county and is a natural gas pipeline, it is to be centrally assessed. The Court

does not feel a physical connection between the various properties is necessary. First, the statute does not require such a physical connection. Further, the statute has examples of centrally assessed properties that are not physically connected, such as railroad car companies, airlines and microwave companies.

Of particular persuasion here is the recent case of PPL Montana, LLC v. Mont. Dep't of Revenue decided by the State Tax Appeal Board in docket numbers SPT-2002-4 and SPT-2002-6. This decision was issued on February 15, 2005. In the PPL case, the issue was whether PPL's property was subject to central assessment. The PPL properties consisted generally of electric generation assets (dams). PPL transmits its energy on transmission lines that are not owned by PPL. PPL contended that since its generation facilities were not physically connected by transmission lines owned by PPL, they were not operated as a single and continuous property. PPL, at 28. The State Tax Appeal Board held:

> The evidence presented at the hearing establishes that PPLM operates its facilities as a single, integrated property. Prior to PPLM's purchase of the generating facilities, they were owned and operated by MPC, which also owned the transmission lines that tie the facilities together. Prior to PPLM's purchase of its generating facilities, MPC operated them as a single, integrated property. Although PPLM did not purchase and therefore does not own the transmission lines, the Purchase Agreement includes an Interconnnection Agreement that permits the generating facilities to continue to operate as a single, integrated property or unit. . . .The express terms of the Interconnection Agreement, and the other evidence and testimony presented at the hearing, establish that PPLM operates its generation facilities as a single, integrated unit, in an efficient and reliable manner, despite the fact that PPLM does not own the transmission lines connecting the facilities as an integrated unit is further facilitated by FERC Order No. 888, which gives PPLM the right to access the transmission system currently owned by NorthWestern, as if PPLM owned the transmission system.

Id., at 28-29.

According to Donkin's testimony, with which this Court agrees, Omimex operates all of its scattered gas fields and pipelines as a single integrated property. The

continuous nature of the property in PPL was provided by the interconnection agreement which allowed PPL to continue to use the transmission lines as if PPL actually owned the transmission lines. According to Donkin, the WPS sales agreement, by which Omimex sells all of its natural gas to WPS, operates as a functional equivalent of the interconnection agreement in PPL. Although Omimex does not have an interconnection agreement with NorthWestern allowing it to use NorthWestern's pipelines, it has its sales agreement with WPS which allows WPS to use those transmission lines on Omimex's behalf.

The Court recognizes its Order on Motion for Partial Summary Judgment issued in this case on August 9, 2005, ruled that ARM 42.22.102(3) was invalid. The Court found that the administrative rule was invalid because the agency added additional types of property to be centrally assessed that were not listed in Section 15-23-101, MCA.

The Montana Supreme Court has held: "The unity of tangible properties such as will support the application of the unit method of assessment is not dependent upon physical connection of the separate pieces of property composing the unit." W. Union Telegraph Co. v. State Bd. of Equalization, 91 Mont. 310, 322, 7 P.2d 551, 552 (1932).

> The true and actual value of plaintiff's property is something more than an aggregation of the values of separate parts of it, operated separately, 'it is the aggregate of the values, plus that arising from a connected operation of the whole; and each part contributes, not merely the value arising from its independent operation, but its mileage proportion of that flowing from a continuous and connected operation as whole."

Id, at 324, 7 P.2d at 553. The supreme court went on to quote the United States Supreme Court:

> Doubtless there is a distinction between the property of railroad

> and telegraph companies and that of express companies. The physical unity existing in the former is lacking in the latter; but there is the same unity in the use of the entire property for the specific purpose, and there are the same elements of value arising from such use. The cars of the Pullman Company did not constitute a physical unity, and their value as separate cars did not bear a direct relation to the valuation which was sustained in that case. . . .The cars were moved by railway carriers under contract, and the taxation of the corporation in Pennsylvania was sustained on the theory that the whole property of the company might be regarded as a unit plant, with a unit value, a proportionate part of which value might be reached by the state authorities on the basis indicated. . . . The unit is a unit of use and management. . . . We repeat that, while the unity which exists may not be a physical unity, it is something more than a mere unity of ownership. It is a unity of use, not simply for the convenience or pecuniary profit of the owner, but existing in the very necessities of the case,--resulting from the very nature of the business.

Id. at 322, 7 P.2d 552-53, *citing* Adams Express Co. v. Ohio State Auditor, 165 U.S. 194, 41 L. Ed. 683, 17 S. Ct. 305, 309. *See, also,* Pullman Palace Car Co. v. Pennsylvania, 141 U.S. 18, 35 L. Ed. 613, 11 S. Ct. 876; Am. Refrigerator Transit Co. v. Hall, 174 U.S. 70, 43 L. Ed. 899, 19 S. Ct. 599; Union Refrigerator Transit Co. v. Lynch, 177 U.S. 149, 44 L. Ed. 708, 20 S. Ct. 631; Union Tank Line v. Wright, 249 U.S. 275, 63 L. Ed. 602, 39 S. Ct. 276; San Francisco-Oakland Terminal Rys. v. Johnson, 210 Cal. 138, 291 P. 197.

Since all of Omimex's Montana properties are functionally operated continuous operation, the Court concludes that Omimex's properties are operating as a single and continuous property in more than one county.

The fact that the Court has ruled that ARM 42.22.102(3) was invalid due to expanding on the statutory scheme does not automatically help Omimex in this case. While the administrative rule may have unnecessarily expanded the statute, the Montana Supreme Court in W. Union Telegraph has indicated that properties, such as Omimex's, do not need to be physically connected in order to support central assessment. That case went on to note that we are to look at unity of use of the entire

property. Thus, even without the administrative rule, prior decisions of the Montana Supreme Court support the DOR's conclusions that Omimex's properties should be centrally assessed since it operates as a single and continuous property.

The question then becomes, if the properties are to be centrally assessed, into what class should the properties be placed? As noted above, the DOR classified Omimex's property, in Section 15-6-141, MCA, as class nine property carrying a 12 percent taxable percentage. The specific language relied on by the DOR is subsection (1)(c) of that statute, which provides: "Class nine properties include: . . . centrally assessed companies' allocations." In this case, the centrally assessed allocation includes that portion of Omimex's properties located in Montana. Please recall that Omimex has property in Canada that is not included in this centrally assessed allocation.

As noted above, Omimex suggests that its properties should be class eight property pursuant to Section 15-6-138, MCA, which provides: "Class eight property includes: . . . all oil and gas production machinery, fixtures, equipment, including pumping units, oil field storage tanks, water storage tanks, water disposal injection pumps, gas compressor and dehydrator units, . . . gas separators, . . . and similar equipment." This class of property carries a 3 percent taxable percentage.

Section 15-6-138, MCA, would apply only if the property were not centrally assessed. For example, it is the understanding of the Court that when this property was owned by MPC and its successors, the property was taxed as class nine property and not as class eight property. Class eight property would be, in the view of the Court, all gas production equipment that was not centrally assessed.

Section 15-6-141, MCA, was enacted as House Bill 643 by the 1979 Montana Legislature. The title of the bill "[a]n Act to require to that all operating

property owned by centrally assessed properties be assessed by the Department of Revenue to apply a single property tax rate to that property." (Emphasis added.) Clearly, the intent of the legislature was to centrally assess all of the company's operating property.

The Court concludes that the DOR has properly centrally assessed all of Omimex's property and has properly taxed it as class nine property to be taxed at the rate of 12 percent of market value.

The attorney for DOR is directed to prepare a judgment incorporating the terms of this decision for the Court's signature.

DATED this 2 day of Feb, 2002.

JEFFREY M. SHERLOCK
District Court Judge

pcs: James P. Sites/Denise Linford
Charlena Toro/Monica L. Smith

T/JMS/omimex v mdor fco.wpd